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United States
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DFAS Needs More Effective Controls
Over Managing DoD Contractor Debt

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Acronyms and Abbreviations

APO	Accounts Payable Office
ARO	Accounts Receivable Office
CAGE	Commercial and Government Entity
CDS	Contractor Debt System
DFAS	Defense Finance and Accounting Service
DoD FMR	DoD Financial Management Regulation
TIN	Taxpayer Identification Number



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

July 15, 2011

MEMORANDUM FOR DIRECTOR, DEFENSE FINANCE AND ACCOUNTING
SERVICE

SUBJECT: DFAS Needs More Effective Controls Over Managing DoD Contractor Debt
(Report No. D-2011-084)

We are providing this report for review and comment. The Contractor Debt System is a database used by the Defense Finance and Accounting Service to manage DoD contractor debt. Defense Finance and Accounting Service did not have proper controls to record and track DoD contractor debts. Specifically, of 141 contractor debt transactions valued at \$124.7 million, the Defense Finance and Accounting Service did not have Taxpayer Identification Numbers and Commercial and Government Entity codes for 46 debt transactions, valued at \$15.7 million, and did not have documentation supporting the appropriation, line of accounting, original principal, or delinquent age attributes for 62 debt transactions, valued at \$58.3 million. We considered management comments on a draft of this report when preparing the final report.

DoD Directive 7650.3 requires that recommendations be resolved promptly. Some of the comments received from the Director, Standards and Compliance, Defense Finance and Accounting Service were only partially responsive. Therefore, we request that the Director, Standards and Compliance provide additional comments to Recommendations 1.a, 1.b, and 1.c.(1) by August 15, 2011.

If possible, send management comments in electronic format (Adobe Acrobat file only) to audclev@dodig.mil. Copies of management comments must have the actual signature of the authorizing official for your organization. We cannot 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
Financial Management and Reporting



Results in Brief: DFAS Needs More Effective Controls Over Managing DoD Contractor Debt

What We Did

We determined whether the Defense Finance and Accounting Service (DFAS) had controls in place to ensure the completeness and accuracy of data in the Contractor Debt System (CDS). Specifically, we determined whether DFAS properly recorded, offset, and tracked contractor debts and collections. We reviewed 141 contractor debt transactions valued at \$124.7 million in the CDS.

What We Found

DFAS management did not effectively manage the completeness and accuracy of data in CDS. For the 141 sample transactions we reviewed, 46 transactions, valued at \$15.7 million, did not have a Taxpayer Identification Number (TIN) and a Commercial and Government Entity (CAGE) code and 62 transactions, valued at \$58.3 million, had insufficient supporting documentation.

DFAS personnel properly offset contractor debts when a valid TIN or CAGE code was available. However, DFAS management did not have controls over recording contractor identification information and did not have effective controls for tracking contractor debts.

DFAS personnel did not properly record or track contractor debt because procedures and system controls did not require a valid TIN and CAGE code to be recorded in CDS. Accounts Receivable technicians also did not have evidence that they validated contractor debt data collected and entered into CDS. As a result, there is an increased risk that DFAS Operations will not collect all of DoD contractor debt.

What We Recommend

We recommend that the Director, Standards & Compliance, DFAS, improve management controls over completeness and accuracy of data in CDS by:

- revising procedures to require the recording of a valid TIN and CAGE code,
- implementing controls over the CDS TIN and CAGE code data fields, and
- requiring technicians to collect all supporting documentation.

We also recommend that the Deputy Director for Operations, DFAS, identify a valid TIN or CAGE code for each debt transaction in CDS currently missing that information.

Management Comments and Our Response

The Director, Standards and Compliance, DFAS provided comments for each recommendation. Not all comments were fully responsive; therefore, we require additional information. We request that the Director, Standards and Compliance, DFAS, reconsider his position and provide additional comments by August 15, 2011. Please see the recommendations table on the back of this page.

Recommendations Table

Management	Recommendations Requiring Comment	No Additional Comments Required
Director, Standards & Compliance, Defense Finance and Accounting Service	1.a, 1.b, 1.c.(1)	1.c.(2)
Deputy Director for Operations, Defense Finance and Accounting Service		2

Please provide comments by August 15, 2011.

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Introduction

Audit Objectives

Our objective was to determine whether the Defense Finance and Accounting Service (DFAS) had controls in place to ensure the completeness and accuracy of data in the Contractor Debt System (CDS). Specifically, we determined whether DFAS properly recorded, offset, and tracked contractor debts and collections. See Appendix A for the scope and methodology. See the Glossary of Technical Terms for definitions of specialized terms.

Background for DFAS Operations

DFAS provides financial and accounting services for DoD, including a debt collection service. DFAS Operations' mission is to provide responsive and professional financial management and accounting, analysis, and consultation services, including accounting, vendor pay, contract pay, and debt management services. A debt to DoD is a receivable that arises from a claim to cash or other assets against another entity.

As of June 30, 2009, contractors were indebted to DoD for \$3.1 billion.¹ DFAS personnel collected \$1.9 billion in debts owed to DoD for FYs 2007 and 2008 and for FY 2009 (as of June 30). When a contractor or vendor² owes a debt to DoD, DFAS Operations manages recording and collecting the debt through the Accounts Payable Office (APO) and the Accounts Receivable Office (ARO). APO initiates the recognition of the debt and then transfers it to ARO. DFAS Operations uses CDS to capture data and documentation related to each contractor debt owed to DoD.

DFAS Operations Uses the Contractor Debt System

CDS is a database developed in 2002 to help manage delinquent accounts receivable from issuing the initial demand letters to collecting the debts. CDS assigns a unique Bill of Collection number to each contractor debt as a debt management tool. CDS allows users to prepare a demand letter from the database, post any additional debt information to the demand letter, and issue the demand letter by hard copy or e-mail.

CDS debt records contain the debt balance, including applicable interest computation and penalties. It maintains the debt status, including debts in litigation, bankruptcy, dispute, or sent to the Department of the Treasury, to assist in account receivable reporting. CDS also identifies invoices eligible for offset, provides reports of actions due by status, and identifies the length of time the debt was in each status.

¹ This information comes from the end-of-month Monthly Debt Management Report for June 2009, as provided by DFAS.

² CDS includes contractor and vendor debts; therefore, we use these terms interchangeably in the report.

Accounts Payable Office

APO technicians disburse funds to DoD contractors through various payment systems. Sometimes these payments include improper payments, duplicate payments, and overpayments made to DoD contractors. DFAS Standards & Compliance standard operating procedures, “Accounts Payable – Accounts Receivable Handoff” (Handoff procedure) outlines the debt management process. When APO technicians identify an erroneous payment using electronic funds transfer, they have 5 business days to recover those funds. Once the 5 days have lapsed, APO technicians must enter the debt into CDS within 5 more days (10 business days after the payment date). However, when APO technicians identify an erroneous payment that was made by issuing a check, they should immediately enter the debt into CDS. When these steps are completed, APO technicians transfer the debt in CDS to ARO technicians by e-mail. APO technicians:

- validate and identify the erroneous payment by type (duplicate or overpayment) and ensure that it has not been collected, offset, or scheduled for an offset within the payment system;
- evaluate the erroneous payment to determine if it meets Loss of Funds criteria³ and notates the Loss of Funds in the CDS notes field; and
- enter the required information into CDS and electronically attaches supporting documentation. Once attached, APO technicians select the Accounts Receivable option and CDS sends an e-mail notification to the Accounts Receivable Office.

Supporting documentation for the erroneous payment entered into CDS should include, but is not limited to, items required by DoD Regulation 7000.14-R, “DoD Financial Management Regulation” (DoD FMR), volume 10, chapter 18, “Contractor Debt Collection.” Supporting documentation should also include items required by the Handoff procedure. See Appendix B for the detailed list of required items.

The contractor’s Taxpayer Identification Number (TIN) and the Commercial and Government Entity (CAGE) code are also required in supporting documentation. DoD FMR, volume 10, chapter 17, “Electronic Submissions and Processing,” states that all contractors are required to provide a TIN, except for foreign contractors doing business outside the United States. In addition, it states that contractors are to provide a CAGE code to receive Prompt Payment interest. A TIN and a CAGE code are necessary for effectively processing debt transactions; when a valid TIN and CAGE code are included in the debt file, DFAS is more effective at collecting the debt through an administrative offset.

³ A debt meets the Loss of Funds criteria when it is a public debt that is 180 days delinquent or when it cannot be collected within 2 years, is from certain source systems, and has one of certain debt reason codes.

Accounts Receivable Office

ARO uses CDS to provide debt reporting and debt management to DoD Components. ARO sometimes uses CDS to reconcile its accounts receivable with its accounting system when compiling the Treasury Report on Receivables. ARO technicians start the due process by issuing the initial demand letter to the debtor. They periodically validate and reconcile the Monthly Debt Management Report to data in the accounting systems as required by the Handoff procedure. Specifically, ARO technicians:

- review the erroneous payment within CDS to determine if it meets the necessary criteria of a debt;
- verify the debt has not been collected;
- establish a receivable in the accounting system based on the information received from APO technicians;
- prepare and send the initial CDS demand letter to vendors within 5 business days after notification of debt from APO technicians;
- follow up on the debt transactions every 30 days or until collection or write-off;
- maintain a record of all telephone conversations and a copy of all supporting documentation, including correspondence, in the respective Debt Management hard copy folders and in the comments section in CDS;
- update CDS daily with the current status of each erroneous payment until collection or write-off;
- notify, on the 31st day, the Vendor Pay Office that they have not received a repayment to initiate offset for the overpayments;
- complete additional activities needed to collect any debt that the Vendor Pay Office could not offset or for which ARO technicians had not received a response from the vendor within the 30 day period established in the initial demand letter;
- transfer to the Debt Management Office delinquent debts that meet the following criteria:
 - o debt is \$600 or more (individually or in aggregate),
 - o the contractor has made no effort to repay the debt, and
 - o 90 days has elapsed from the initial demand letter.

See Appendix C for a flowchart of the debt management process.

Internal Controls for Contractor Debt Management

DoD Instruction 5010.40, “Managers’ Internal Control Program (MICP) Procedures,” July 29, 2010, requires DoD organizations to implement a comprehensive system of internal controls that provides reasonable assurance that programs are operating as intended and to evaluate the effectiveness of the controls. DFAS management had procedures to validate data and supporting documentation as part of their internal controls for contractor debt management; however, DFAS management did not have controls over recording contractor identification information and did not have effective controls for tracking contractor debts. We will provide a copy of the final report to the senior official responsible for internal controls in DFAS Operations.

Finding. DFAS Needs to Comply With Contractor Debt Management Requirements

DFAS management did not effectively manage the completeness and accuracy of data in CDS. Specifically, DFAS management did not have controls for recording contractor identification information and did not have effective controls for tracking contractor debts. For 141 sample contractor debt transactions valued at \$124.7 million, DFAS personnel did not have:

- TINs and CAGE codes for 46 debt transactions, valued at \$15.7 million, and
- documentation supporting the appropriation, line of accounting, original principal, or delinquent age attributes for 62 debt transactions,⁴ valued at \$58.3 million.

DFAS personnel did not properly record or track contractor debt because the Handoff procedures, the CDS User Manual, and system controls did not require a valid TIN and CAGE code to be recorded in CDS. Technicians also did not have evidence that they validated contractor debt data collected and entered into CDS. As a result, there is an increased risk that DFAS Operations will not collect all of DoD contractor debt. For example, without a correct TIN and CAGE code in CDS, DFAS management continues to be unable to collect an additional \$3.2 million in debt for 19 of 46 debt transactions.

Contractor Debt Transactions Reviewed

DFAS personnel recorded debts in eight Accounting Status categories: (1) At Justice, (2) Bankruptcy, (3) Dispute, (4) Litigation, (5) Treasury, (6) Forbearance, (7) Other, and (8) Closed. Categories 1 through 6 were outside the control of the Accounts Receivable Office (ARO). Debts categorized as “Other”⁵ are considered collectible and remain under ARO control. We based the scope of this audit on “Other” contractor debt transactions in CDS. “Other” debts totaled \$134.9 million in FY 2007, \$264.2 million in FY 2008, and \$209.3 million as of June 30, 2009.

APO Needs to Record Valid Contractor Identification Data

DFAS management did not have controls for recording contractor identification information. ARO technicians provided supporting documentation for 141 contractor debt transactions sampled, valued at \$124.7 million. However, only 94 of those contractor debt transactions, valued at \$108.2 million, included either a valid TIN or a valid CAGE code because APO technicians did not properly record contractor

⁴ Of these contractor debt transactions, 14 (valued at \$9.3 million) are included in the 46 contractor debt transactions with invalid TIN and CAGE codes.

⁵ To match Department of Treasury reporting elements, CDS includes active contractor debts under the category of “Other.”

identification information. Two fields in CDS identify contractors: the TIN and the CAGE code. APO technicians did not properly enter the TIN or CAGE code in CDS because the Handoff procedures, CDS User Manual, and system controls did not specifically require a valid entry for either field.

DFAS management did not have controls over identifying and entering contractor identification information in CDS to effectively process debt collection.

DFAS management did not have controls over identifying and entering contractor identification information in CDS to effectively process debt collection. DoD FMR, volume 10, chapter 17, requires organizations to identify a contractor TIN in the payment process. In addition, in accordance with DoD FMR, volume 10, chapter 18, APO

technicians can collect a debt owed to DoD by completing an administrative offset. When offsetting a debt, APO technicians make a deduction from a current payment due to that contractor for the amount of the debt owed to DoD. APO technicians cannot perform an administrative offset without the contractor's TIN or CAGE code. DoD Instruction 5010.40, "Managers' Internal Control (MIC) Procedures," states that:

[A] Managers' Internal Control Program be established to review, assess, and report on the effectiveness of Internal Controls in the Department of Defense. The Managers' Internal Control Program shall identify and promptly correct ineffective Internal Controls, and establish Internal Controls.

APO management should have procedures to ensure that TINs and CAGE codes are properly recorded for all established debts to allow ARO management to efficiently monitor and report DoD contractor debt. When a valid TIN and CAGE code are present, ARO technicians can better identify the debtor and collect the debt through offset. For example, DFAS personnel have effectively collected a portion of seven debts in our sample valued at \$21.1 million, through an administrative offset. The Handoff procedures did not require a valid TIN or CAGE code to be recorded in CDS. In addition, the CDS User Manual stated only that APO should make every attempt to research and fill the TIN field, as it would be critical later in the process.

DFAS management did not ensure CDS system controls required valid entries. For example, CDS:

- did not require the TIN field to be populated, and it defaulted to "000000000;"
- did not require a valid CAGE code field to be populated; and
- allowed alphabetic character entries, such as "none," in both fields.

Without a valid TIN or CAGE code, ARO technicians could not follow proper procedures that enabled them to process debts.

Therefore, technicians could ignore the fields or input invalid entries. TINs and CAGE codes are necessary in the debt collection process to provide technicians all collection options.

ARO technicians stated that APO technicians did not always provide the TIN or CAGE code. Without a valid TIN or CAGE code, ARO technicians could not follow proper procedures that enabled them to process debts. Instead, they performed additional research to identify valid TIN and CAGE codes. As a best practice, APO technicians should identify and record a TIN and CAGE code when initially entering the contractor debt into CDS.

From our sample of 141 debt transactions, 46 debt transactions, valued at \$15.7 million, as of June 30, 2009, did not have a valid TIN and CAGE code. As of February 1, 2010, of these 46 transactions, 26 transactions⁶, valued at \$13.2 million, had moved outside of ARO control, and 19 transactions, valued at \$3.2 million, were still categorized as “Other.” If they had recorded a valid TIN and CAGE code in CDS, APO technicians may have greatly increased ARO’s ability to collect 19 debt transactions, valued at \$3.2 million.

We analyzed the entire population of the “Other” contractor debt transactions contained in CDS, as of February 1, 2010, and found that 1,536 out of 7,124 debt transactions, valued at \$34 million and \$308.1 million, respectively, did not have valid TINs and CAGE codes. Invalid TIN and CAGE codes increase the risk that ARO technicians will not collect the debt owed to the DoD and may not properly offset debts.

To improve technicians’ ability to collect debt, the Director, Standards & Compliance, DFAS, should:

- revise its Handoff procedures to require APO technicians to identify valid TIN and CAGE codes and enter them when initially generating the contractor debt record in CDS, and
- implement controls in CDS to make the TIN and CAGE code data fields required fields to ensure that APO technicians do not establish debts without having a valid TIN or CAGE code.

For APO technicians to be capable of offsetting debts in CDS, the Deputy Director for Operations, DFAS, should research and identify a valid TIN or CAGE code for each debt transaction in CDS currently missing that information.

ARO Needs to Effectively Track Contractor Debt

ARO management did not have effective controls for tracking contractor debts.

ARO management did not have effective controls for tracking contractor debts. DoD FMR, volume 10, chapter 18, and the Handoff procedures provide lists of the documentation⁷

⁶ The contractor debt transactions mentioned here represent 45 transactions, valued at \$16.4 million, because some debt transaction amounts had been adjusted or combined.

⁷ See Appendix B for the lists of documentation needed.

that APO technicians should collect and ARO technicians should use to verify data entered into a contractor debt transaction in CDS. In addition, according to the “Monthly Debt Management Report Reconciliation Procedures,” October 28, 2009, ARO technicians are to validate and reconcile to the accounting systems’ debt records as they are received. ARO technicians are to perform status reviews every 120 days to ensure that the accounting systems and CDS remain in balance. However, ARO technicians did not include evidence in the contractor debt folder that they had validated the data APO technicians entered into CDS.

We reviewed 141 contractor debt transactions to determine the accuracy of data in four CDS attributes: Appropriation, Line of Accounting, Original Principal, and Delinquent Age.

- **Appropriation Number and Line of Accounting** - The Appropriation Number contains a 2-digit Treasury Index Symbol, 2-digit Fiscal Year, and 4-digit Basic Symbol obtained from an invoice or voucher related to the debt. The Line of Accounting contains information used to accumulate appropriation, budget, and management information related to the debt.

The Appropriation Number, in conjunction with the Line of Accounting, indicates where the funds originated from (the appropriation or other source) and, where the funds should be returned upon collection. If they do not have the correct Appropriation Number and Line of Accounting, ARO technicians could return the funds to the incorrect source and create a potential misappropriation of funds.

- **Original Principal** - The Original Principal shows the debt amount in CDS. It is the original amount of the debt. This amount is important in ensuring that ARO technicians collect the proper amount owed to DoD.
- **Delinquent Age** - The Delinquent Age shows whether ARO technicians followed the required timeline for due process. It is the age of the debt from the date of the initial demand letter to the date the debt is closed. The age of the debt is used to determine when certain events are to occur during collection. For instance, 90 days after the initial demand letter is provided to the debtor, ARO technicians should transfer the debt to the Debt Management Office for collection if they have not received a response from the debtor. Further, 90 days after the Debt Management Office receives the debt, it should turn the debt over to a private collection agency or to the Department of the Treasury if it has not received a response from the debtor.

We compared the attribute data in CDS to the data in the supporting documentation and identified 62 unsupported contractor debt transactions valued at \$58.3 million. The 62 unsupported contractor debt transactions resulted in 114 unsupported attributes. For example, one transaction for \$2.1 million had incorrect data in all four attributes. Another transaction for \$12.5 million had an unsupported delinquent age attribute. See Appendix D for detail regarding unsupported contractor debt transactions. The following

table summarizes the number of instances that we identified insufficient documentation to support the data in CDS for the four attributes.

Contractor Debt Transaction Attribute Testing Results	
Attribute	Not Supported
Appropriation Number	27
Line of Accounting	37
Original Principal	19
Delinquent Age	31
Total	114

According to the CDS User Manual, personnel can link supporting documentation for the related debt transactions to CDS when personnel save the documentation on a common network drive. Readily available electronic supporting documentation would allow the technician to quickly retrieve the specific documents for each contractor debt transaction.

Without sufficient controls in place to verify the debts with complete supporting documentation, ARO management increased the risk that they will not be able to collect contractor debt. ARO has a 120-day periodic review process in place. During these periodic reviews, the Director, Standards & Compliance, should further require ARO technicians to validate that evidence supporting the debt has been collected and linked to the debts already recorded in CDS. If the review finds unsupported debts, immediate action should be taken to fully support the debts in CDS. DFAS personnel should collect and use the types of documents found in the DoD FMR, volume 10, chapter 18, and the Handoff procedures (see Appendix B).

Recommendations, Management Comments, and Our Response

1. We recommend that the Director, Standards & Compliance, Defense Finance and Accounting Service, improve controls over completeness and accuracy of data in the Contractor Debt System by:

a. Revising standard operating procedures, “Accounts Payable - Accounts Receivable Handoff,” and the CDS User Manual to require the Accounts Payable Office to record the Taxpayer Identification Number and the Commercial and Government Entity code in the Contractor Debt System when initially generating the contractor debt record.

Defense Finance and Accounting Service Comments

The Director, Standards & Compliance, DFAS, agreed and stated that the Handoff procedures, Contract Debt System Desktop Guide, and Contract Debt System Manual 8-2010 include the requirement to populate the TIN and CAGE code fields.

Our Response

We considered the Director, Standards & Compliance, DFAS, comments nonresponsive. Although DFAS agreed with the recommendation, DFAS stated that the requirement to populate the TIN and CAGE code fields was already contained in the guidance. We disagree; there is no language in the Handoff procedures or other supporting documentation stating the APO technicians must obtain and enter the TIN and CAGE code into CDS. For example, the Contract Debt System Desktop Guide states, “Complete the Contractor Information on the Checklist For New Account Record screen, as applicable.” It does not specifically state that APO technicians must obtain and enter the TIN and CAGE code for the contractor. In addition, the Contract Debt System Desktop Guide shows a CDS screen shot showing the default entries for the TIN (000000000) and CAGE code (None). We ask that the Director, Standards & Compliance, DFAS, revise the Handoff procedures, and any other guidance or instructions, to include stronger language to require the TIN and CAGE code are completed in CDS.

b. Implementing controls in the Contractor Debt System that require valid data entries for the Taxpayer Identification Number and Commercial and Government Entity code data fields.

Defense Finance and Accounting Service Comments

The Director, Standards & Compliance, DFAS, did not agree with this recommendation. He stated that the recommendation was redundant and that recommendation 1.a addressed the “accuracy” of the TIN and CAGE code.

Our Response

We considered the Director, Standards & Compliance, DFAS, comments nonresponsive. The Director, Standards & Compliance, DFAS, should place restrictions on the TIN and CAGE code data fields in CDS, so that APO technicians enter the proper number and type of characters into each field, and so a default value is no longer included in either field. This would implement a change to the system to provide a two-pronged approach, ensuring that APO technicians enter the data and enter it correctly. Currently, Contract Debt System Manual 8-2010, instructs APO technicians to enter the TIN and CAGE code and, if either is unknown, to leave the default of “None” or enter all zeros (000000000). We ask that the Director, Standards & Compliance, DFAS, establish restrictions on the TIN and CAGE code data fields within CDS to ensure accuracy.

c. Requiring Accounts Payable Office and Accounts Receivable Office technicians to collect:

(1) supporting documentation that conforms to the DoD Financial Management Regulation, volume 10, chapter 18, and Defense Finance and Accounting Service Standards & Compliance standard operating procedure, “Accounts Payable - Accounts Receivable Handoff;”

Defense Finance and Accounting Service Comments

The Director, Standards & Compliance, DFAS, agreed and stated that the Handoff procedures and “Monthly Debt Management Report Reconciliation Procedures,” October 28, 2009, provide specific steps required when there is insufficient documentation.

Our Response

We considered the Director, Standards & Compliance, DFAS, comments nonresponsive. Although DFAS agreed with the recommendation, DFAS stated that the requirement for APO technicians collect the supporting documentation necessary to initiate a contractor debt transaction was already contained in the guidance. We disagree; currently, the Handoff procedures include a list of documentation that will be included in the erroneous payment package. The Handoff procedures do not specify what the APO technicians need to initiate a debt transaction. We ask that the Director, Standards & Compliance, DFAS, revise the Handoff procedures to include a specific list of documentation needed to support the initiation of a contractor debt transaction in CDS.

(2) evidence of verification made during the current periodic review to confirm that complete supporting documentation is available and linked in the Contractor Debt System when debts are established. If the periodic review identifies that supporting documentation is insufficient and not linked to the debt record, technicians should take immediate action to fully support the debt recorded in the Contractor Debt System.

Defense Finance and Accounting Service Comments

The Director, Standards & Compliance, DFAS, agreed and stated that his office established the Sampling of Transactions Metric to ensure all documents are linked to CDS as of January 2011. Further, Standards & Compliance–ARO Site Points of Contact are to verify that documents are linked to CDS and notify the site when and if documents are missing or fields are not supported.

Our Response

We considered the Director, Standards & Compliance, DFAS, comments responsive. The Director, Standards & Compliance, DFAS, implemented the Sampling of Transactions Metric that provides another level of review of the documentation supporting the contractor debt transactions in CDS. We require no additional comments

2. We recommend that the Deputy Director for Operations, Defense Finance and Accounting Service, identify valid Taxpayer Identification Number and Commercial and Government Entity codes for each debt transaction in the Contractor Debt System currently missing that information.

Defense Finance and Accounting Service Comments

The Director, Standards & Compliance, DFAS, responded for the Deputy Director for Operations, DFAS. He agreed and stated that all debts are required to be reviewed in

CDS every 120 days, adding that, based on the numbers monitoring this requirement, improvements are required to ensure compliance. Standards & Compliance, DFAS Accounts Receivable, will organize an initiative for the AROs to populate all missing TIN and CAGE codes for valid open debts, and those with missing TIN and CAGE codes determined to be invalid debts will be closed in CDS.

Our Response

We considered the Director, Standards & Compliance, DFAS, comments responsive. It is our understanding that Standards & Compliance, DFAS personnel, will not close debts in CDS without first following procedures to collect the debt or write the debts off in accordance with DoD Financial Management Regulation, volume 4, chapter 3. We require no additional comments.

Appendix A. Scope and Methodology of Audit

We conducted this performance audit from September 2009 through April 2011 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 finding and conclusion based on our audit objectives.

We based the scope of this audit on the “Other” contractor debt transactions from the Monthly Debt Management Report for the period ending June 30, 2009. DFAS management uses CDS to produce the Monthly Debt Management Report for management’s review of debt collection status. The Monthly Debt Management Report contained a total population of 8,848 “Other” contractor debt transactions valued at \$209.3 million, as of June 30, 2009. We selected a statistical sample of 150 contractor debt transactions valued at \$124.7 million for review. Nine sample transactions valued at \$1,946 were excluded because other DoD reviews were on-going with these contractor debt transactions. See Appendix E for a complete discussion of our sampling methodology.

We performed this audit at DFAS centers in Cleveland, Ohio; Columbus, Ohio; Indianapolis, Indiana; Limestone, Maine; and Rome, New York. For each site, we reviewed supporting documentation for contractor debt transactions and walked through procedures for recording debts in CDS.

Use of Computer-Processed Data

To perform this audit, we obtained and analyzed data from the Monthly Debt Management Report. We reconciled data from the Monthly Debt Management Report to a data query from CDS that DFAS personnel ran the same day. As a result, we determined that the data from the Monthly Debt Management Report was a fair representation of the data contained in CDS and, therefore, was sufficiently reliable for the purpose of our review.

Use of Technical Assistance

The DoD IG Quantitative Methods and Analysis Division provided technical assistance throughout the sample selection and analysis process. See Appendix E for a detailed description of the sampling methodology provided by the Quantitative Methods and Analysis Division.

Prior Coverage of Contractor Debt

During the last 5 years, the Government Accountability Office (GAO) and DoD IG have issued two reports discussing contractor debt. Unrestricted GAO reports can be accessed over the Internet at <http://www.gao.gov>. Unrestricted DoD IG reports can be accessed at <http://www.dodig.mil/audit/reports>.

GAO

GAO Report No. GAO-09-442, "Significant Improvements Needed in DoD's Efforts to Address Improper Payment and Recovery Auditing Requirements," July 2009

DoD IG

DoD IG Report No. D-2008-046, "Defense Finance and Accounting Service Compliance with the Debt Collection and Improvement Act of 1996 for the Department of the Navy," February 6, 2008

Appendix B. Required Supporting Documentation

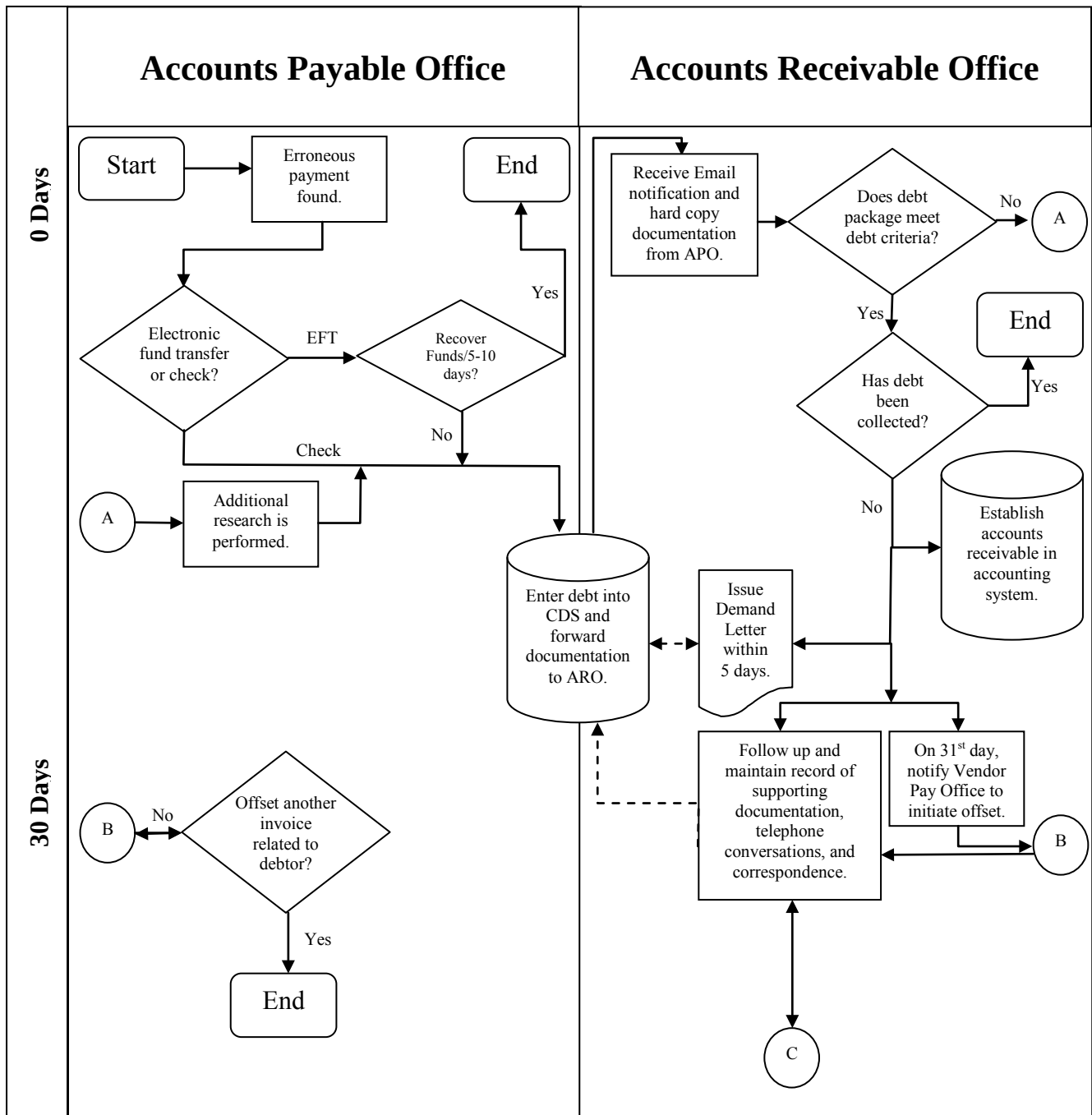
The DoD FMR, volume 10, chapter 18, requires supporting documentation (listed below) to minimally support a debt.

DoD Financial Management Regulation, volume 10, chapter 18, “Contractor Debt Collection”
Copies of paid vouchers, which relate to the specific debt.
Amounts and dates of collections that were received or payments that were offset.
For duplicate payments and dual negotiated successor checks, copies of the negotiated checks obtained from the Department of the Treasury.
All demand letters, other correspondence, and written documentation of telephone or personal contact with the debtor and others, which are pertinent to the debt.
Any other documents needed to support a recommendation for compromise, discontinuance, or termination.
The accounting classification or appropriation to which the principal portion of the payments should be deposited.
Taxpayer Identification Number.
Telephone number, address, and the name of a point of contact who is knowledgeable of the following entities: a. Debtor. b. Contracting office making the referral. c. Disbursing office making the referral. d. Supporting accounting office.
In the case of a determination of debt(s) resulting from an audit or contract reconciliation, a copy of the audit or reconciliation report with sufficient supporting documentation to explain the conclusions.
Copies of documentation supporting sales of goods and services to commercial entities on a reimbursable basis.
The Commercial and Government Entity code.

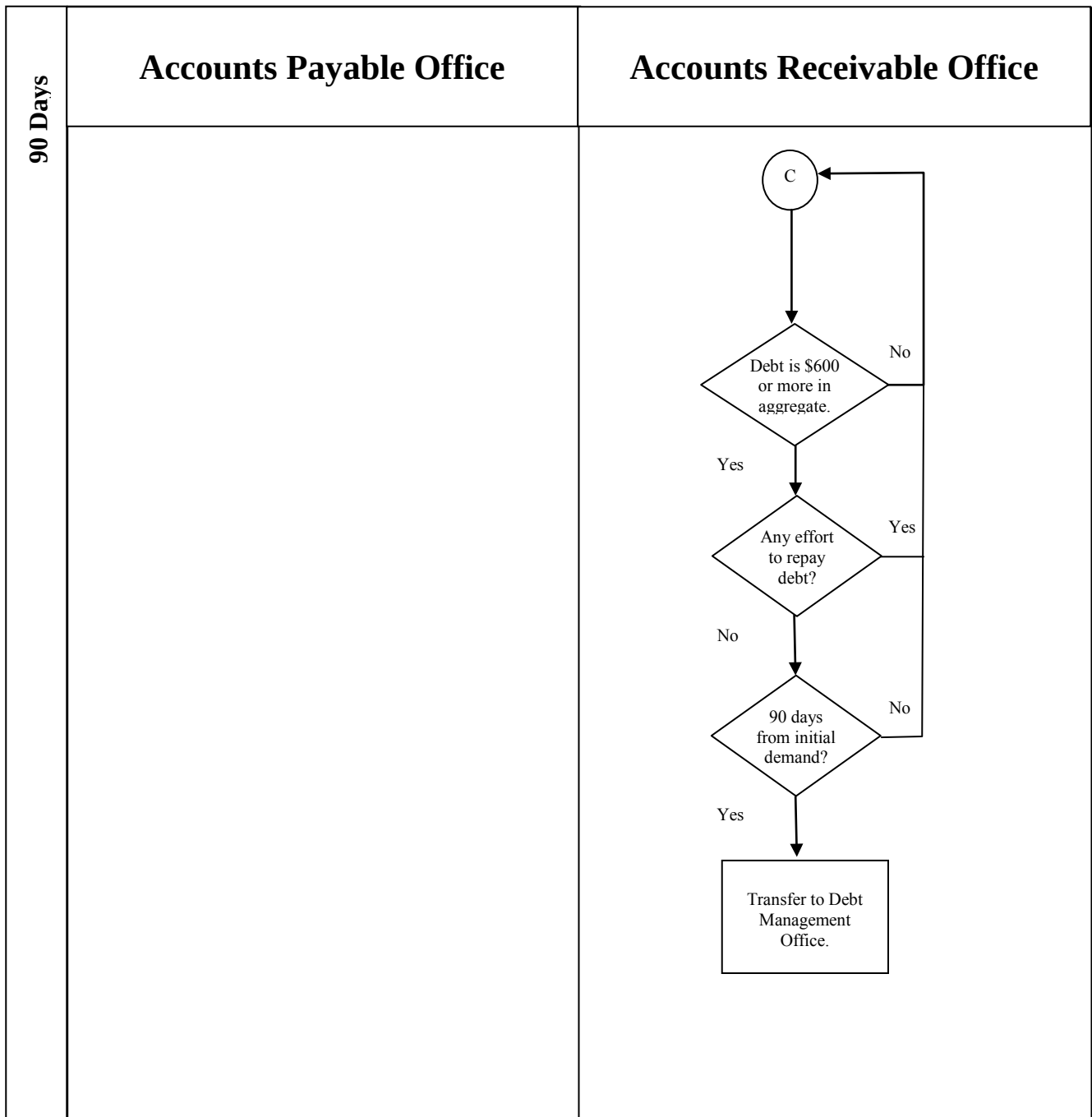
The DFAS Standards & Compliance Handoff procedures require specific documentation (listed below) to ensure the proper accounting recognition, due diligence, and debt management functions are performed and standardized across all the DFAS Sites.

DFAS Standards & Compliance, standard operating procedures, “Accounts Payable – Accounts Receivable Handoff”
Invoice(s).
Check or Electronic Funds Transfer trace-number to include account number and name of the bank.
Contract and modification if not in Electronic Data Access (if applicable).
Detailed explanation of how the erroneous payment occurred.
Date of the erroneous payment was discovered and who discovered it.
Any audit results or other supporting documentation pertinent to the erroneous payment.
A printout of the CDS Main Record Screen to include the Bill of Collection number.

Appendix C. Debt Management Flowchart



Note: Continues Next Page



Appendix D. Attribute Testing Results

Count	Bill Of Collection	Appropriation	Line of Accounting	Original Principal Amount	Delinquent Age	Original Principal Dollar Amount
1	09126090125C1				X	\$12,463,600.00
2	08134095526C1		X	X		5,885,297.09
3	09066113102C65				X	5,021,430.56
4	09153132745C1		X			4,849,748.00
5	08134100151C1	X	X			4,805,382.71
6	0636580	X	X			3,295,305.00
7	09066113102C65	X	X	X	X	2,146,336.00
8	07155133411C1	X	X	X		1,534,767.84
9	08115152747C63	X	X	X	X	1,380,215.84
10	0784C18	X	X			1,156,178.35
11	0784C18		X			1,056,058.19
12	0579500441	X	X	X	X	931,093.51
13	09167102536C1	X	X			804,795.14
14	09048102835C1	X	X		X	801,000.00
15	09078112907C65	X	X	X	X	787,398.62
16	06828C1				X	686,640.60
17	09141134528C1	X	X			669,722.00
18	09089102027C1	X	X	X	X	641,178.19
19	08151130311C17				X	634,543.71
20	09161085430C65	X	X	X	X	633,472.25
21	09159131354C65				X	628,550.00
22	09177144338C63		X		X	618,679.92
23	07120095137C63	X	X	X		583,210.00
24	051004LT1	X				554,931.00
25	09170073507C65		X			507,063.32
26	09167115540C1	X	X	X		480,519.36
27	08191143241C1				X	446,470.51
28	07164135156C1		X		X	443,507.05
29	062133C55				X	399,043.00
30	077543C1	X	X	X		356,038.40
31	04151LT1		X			289,856.00
32	078452C63				X	276,088.15
33	0434795				X	274,586.09
34	062890C63		X			259,405.56
35	07214082054C1			X		208,858.00
36	078877C1	X	X			155,986.50
37	09166105619C1	X	X			154,008.00
38	0536085				X	142,345.55
39	09104113709C65			X		132,128.06
40	9710002861		X			131,205.01

Count	Bill Of Collection	Appropriation	Line of Accounting	Original Principal Amount	Delinquent Age	Original Principal Dollar Amount
41	08078075802C1	X	X			125,561.00
42	07227154034C63	X	X	X		117,975.87
43	09317112253C55	X			X	117,698.32
44	08078075802C1	X	X			115,793.00
45	09110103130C1	X	X	X		115,792.35
46	08355132643C27			X		101,429.04
47	08144142313C63				X	65,313.80
48	0536084				X	63,459.72
49	09139105717C27				X	50,000.00
50	09133100400C1	X	X	X		48,640.80
51	09054102120C65				X	22,162.14
52	09138093220C63	X	X	X		16,845.95
53	063637C55		X			16,456.63
54	09148081023C40				X	14,912.86
55	07186121140C65				X	13,223.72
56	07128111410C65	X	X	X	X	13,125.00
57	09350145426C65		X			11,133.67
58	08206104124C65				X	2,602.59
59	09153104525C65				X	2,250.00
60	09133095813C65				X	1,962.50
61	09068134602C65				X	1,296.24
62	09167094826C27		X			483.91
Total		27	37	19	31	\$58,264,762.19

Appendix E. Sampling Methodology

Sampling Purpose

We used a stratified sampling plan developed by the DoD IG Quantitative Methods and Analysis Directorate to determine the number of “Other” contractor debt transactions. The results of our testing allowed us to determine whether internal controls over contractor debt management were working.

Sample Design

We applied stratified sampling to debt transactions included in the “Other” category. The Quantitative Methods and Analysis Directorate designed a stratified sampling design that stratified the population of the “Other” category into four strata and selected the sample shown in the table.

Population and Sample Breakdown for “Other” Transactions		
Stratum	Population Size	Sample Size
≥ 500K	40	40
≥ 100K to <500K	241	50
≥10K to <100K	1,227	40
<10K	7,338	20
Total	8,846	150

The Quantitative Methods and Analysis Directorate personnel based the plan on a 95-percent confidence interval. The audit team reviewed documentation supporting the debt transactions:

- TIN;
- CAGE code;
- appropriation;
- line of accounting;
- original principal; and
- delinquent days, using the date of the initial demand letter.

Glossary of Technical Terms

Admin [Administrative] Write Off. An accounting action that results in reporting the debt/receivable as having no value on the agency's financial and management reports.

Commercial and Government Entity Code. A 5-digit code that identifies contractors doing business with the Federal Government, which is assigned and maintained by the Defense Logistics Information Service.

Due Process. A course of formal proceedings carried out regularly and in accordance with established rules and principles.

Duplicate Payment. A payment that APO makes more than once for the same amount and with the same supporting documentation for each of more than one payment.

Erroneous Payment. A payment that is improper, including duplicate and over payments.

Final Settlement. A debt that has been paid in full or paid in full with an agreed upon compromise.

Improper Payment. All erroneous payments are improper payments. An improper payment is:

- any payment made in an incorrect amount under statutory, contractual, administrative, or other legally applicable requirements;
- made to an ineligible recipient or for an ineligible service, duplicate payments, and payments for services not received; and
- when a Component is unable to determine whether a payment was proper because of insufficient or lack of documentation, this payment must also be considered an error.

Monthly Debt Management Report. A monthly accounts receivable report that the CDS generates for the field sites to include in their quarterly receivable reports.

No Claim. Examples of “No Claim” debts include:

- a debt that is created that has an erroneous appropriation, thus resulting in a new debt transaction;
- a duplicate debt in CDS, resulting in the deletion of the debt transaction; and
- a debt that has been cancelled.

Offset. Withholding funds payable by the U.S. Government to an entity to satisfy a debt that the entity owes the U.S. Government.

Other. To match Department of Treasury reporting elements, CDS includes active contractor debts under the category of “Other.”

Overpayment. An amount that APO pays to a vendor in excess of what the vendor was entitled to receive.

Taxpayer Identification Number. A 9-digit number, which is either an Employer Identification Number assigned by the Internal Revenue Service or a Social Security number assigned by the Social Security Administration.

Treasury Report on Receivables. A quarterly report of public receivables prepared in compliance with the Department of the Treasury guidance. It summarizes the status and condition of the total receivable portfolio from public sources.

Defense Finance and Accounting Service Comments



DEFENSE FINANCE AND ACCOUNTING SERVICE
ARLINGTON
1851 SOUTH BELL STREET
ARLINGTON, VA 22240-5291

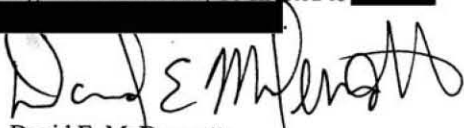
MAY 09 2011

MEMORANDUM FOR DIRECTOR, DEFENSE FINANCIAL AUDITING SERVICE,
OFFICE OF THE INSPECTOR GENERAL, DoD

SUBJECT: DFAS Comments to DoDIG Draft Report, "DFAS Needs More Effective Controls
over Managing DoD Contractor Debt," dated April 8, 2011, Project No. D2009-
D000FN-0300.000

Attached are management comments to DoDIG Draft Report, "DFAS Needs More
Effective Controls over Managing DoD Contractor Debt," dated April 8, 2011, to
recommendations 1a, 1b, 1c, and 2.

Questions your staff may have concerning these matters may be directed to [REDACTED]


David E. McDermott
Director, Standards & Compliance

Attachment:
As stated

www.dod.mil/dfas
Your Financial Partner @ Work

**Management Comments
On
“DFAS Needs More Effective Controls over Managing DoD Contractor Debt”
Project No. D2009-D000FN-0300.000, Dated April 8, 2011**

Recommendation 1a: Director, Standards & Compliance, Defense Finance and Accounting Service (DFAS), improve controls over completeness and accuracy of data in the Contractor Debt System (CDS) by revising standard operating procedures, “Accounts Payable – Accounts Receivable Handoff,” and the CDS User Manual to require the Accounts Payable Office to record the Taxpayer Identification Number and the Commercial and Government Entity code in the Contractor Debt System when initially generating the contractor debt record.

Previous Management Comments: NA

Prior Estimated Completion Date: NA

Current Management Comments: Concur, in October 2009, Standards & Compliance – Accounts Receivable Office released the Accounts Payable (AP)/Accounts Receivable (AR) Handoff Standard Operating Procedures (SOP) which includes populating the TIN & CAGE code fields in Section 3, Page 15. This requirement is also listed in the Contract Debt System (CDS) Desktop Guide in Section “Creating a New Debt Record”, Page 2-7, Step 5 as well as the Contract Debt System (CDS) Manual, 8-2010 in Section “Creating a New Debt Record”, Page SG-2-9, Steps 1 and 2.

Estimated Completion Date: Closed.

Recommendation 1b: Director, Standards & Compliance, Defense Finance and Accounting Service (DFAS), implement controls in the Contractor Debt System that require valid data entries for the Taxpayer Identification Number and Commercial and Government Entity code data fields.

Previous Management Comments: NA

Prior Estimated Completion Date: NA

Current Management Comments: Recommendation is redundant. Item 1a addresses the “accuracy” of the TIN and CAGE.

Completion Date: Closed.

Recommendation 1c: Director, Standards & Compliance, Defense Finance and Accounting Service (DFAS), requiring Accounts Payable Office and Accounts Receivable Office technicians to collect: (1) supporting documentation that conforms to the DoD Financial Management

Regulation, Volume 10, Chapter 18, and Defense Finance and Accounting Service Standards & Compliance standard operating procedure, "Accounts Payable – Accounts Receivable Handoff;" (2) evidence of verification made during the current periodic review to confirm that complete supporting documentation is available and linked in the Contractor Debt System when debts are established. If the periodic review identifies that supporting documentation is insufficient and not linked to the debt record, technicians should take immediate action to fully support the debt recorded in the Contractor Debt System.

Previous Management Comments: NA

Prior Estimated Completion Date: NA

Current Management Comments: Concur, procedures are included in both documents provided to the auditors. For example, the AP/AR Handoff provides specific steps required when insufficient documentation is uploaded by AP, section 2.4 b. 1. In addition, the MDMR Reconciliation Procedures discusses the necessary steps for insufficient supporting documentation on page 5. The "Sampling of Transactions" Metric was established to ensure all documents are loaded into CDS as of January 2011. Standards & Compliance – AR Site POC's verify the documents are loaded in CDS and notifies the site when and if documents are missing or fields are not supported.

Completion Date: Closed.

Recommendation 2: Deputy Director for Operations, Defense Finance and Accounting Service (DFAS), identify valid Taxpayer Identification Number and Commercial and Government Entity codes for each debt transaction in the Contractor Debt System currently missing that information.

Previous Management Comments: NA

Prior Estimated Completion Date: NA

Current Management Comments: Concur, all debts are required to be reviewed in CDS every 120 days. Based on the numbers monitoring this requirement, improvements are required to ensure compliance. S&C Accounts Receivable will organize an initiative for the Accounts Receivable Office(s) to populate all missing TIN and CAGE fields for valid open debts. Debts with missing TIN and CAGE fields determined to be invalid will be closed in CDS.

Estimated Completion Date: September 2011



Inspector General Department of Defense

