



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2884

REPORT NO. 90-092

July 2, 1990

MEMORANDUM FOR DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Final Quick-Reaction Report on the Audit of the
Procurement of Contract Reconciliation Services by
the Defense Logistics Agency (Project No. 0CH-0040.01)

Introduction

In January 1990, we announced the Audit of the Procurement of Contract Reconciliation Services by the Defense Logistics Agency (DLA). The audit objective was to evaluate the DLA's procedures for contracting for support services to reconcile obligations and disbursements on contracts to be transferred for payment from the Defense Contract Administration Services Regions (DCASR) to the Defense Finance Center in Columbus, Ohio. During the audit, we identified two conditions that require immediate attention.

First, DLA has contracted with Coopers and Lybrand, a large Certified Public Accounting firm, to reconcile DoD contracts. Some of these contracts may be with Coopers and Lybrand's audit clients for which they also perform audit or management consulting services. Requiring Coopers and Lybrand to perform the reconciliations could constitute a conflict of interest. The existing affiliation between Coopers and Lybrand and its audit clients might cause the firm to make recommendations or interpretations that could benefit its contractor clients at the expense of the Government. Contracting officials should avoid contracting actions that give the appearance of conflicts of interest, which could be prejudicial to the interest of the United States. The financial reconciliation of DoD contracts places Coopers and Lybrand in a position where it will directly influence obligations and disbursements of the U.S. Government.

Second, DLA did not consider the procurement of reconciliation services to be contracted advisory and assistance services (CAAS), and did not plan to report the contract as CAAS for inclusion in DoD's quarterly report. The management and oversight of CAAS has been a subject of concern to both Congress and the Executive Branch since the early 1980's because it is an area vulnerable to waste and abuse, and because some agencies have grown too dependent on contractors to perform work that is more appropriately performed by Government personnel. Because of this concern, the FY 1990 DoD Appropriations Act placed a limitation on CAAS expenditures and contained a provision that requires DoD to report CAAS obligations quarterly to the Congress

and to the Comptroller General. If DLA does not report the procurement to DoD, DoD's expenditures for CAAS will be understated.

The activities contacted or visited are shown in Enclosure 2.

Background

In April 1989, DLA issued a sole-source letter contract (DLAHOO-89-D-0010) to Network Solutions, Inc., (NSI) through the Small Business Administration 8(a) program. The contract was for NSI to provide automatic data processing and telecommunication support for the transition of finance and accounting operations from nine DCASRs to the Defense Finance Center in Columbus, Ohio. In August 1989, DLA issued Task Order No. 6 to NSI to reconcile over 4,000 selected contracts for transfer from DCASR, Los Angeles, California. NSI subsequently subcontracted with Coopers and Lybrand to reconcile the contracts. Work under the original contract with NSI and Coopers and Lybrand is largely complete. The total value of the contract with NSI is about \$24.6 million, of which approximately \$4.4 million is attributable to contract reconciliation work.

On April 6, 1990, DLA awarded a follow-on contract (DLA600-90-D-5047) to Coopers and Lybrand to reconcile contracts at the other eight DCASRs. The estimated total value of this contract is \$15.0 million.

The contracts to be reconciled are with private-sector firms that provide goods and services to DoD. The reconciliation process requires that Coopers and Lybrand's staff review contract modifications, contractor invoices, payment vouchers and other documents, validate the disbursements and obligations on the contracts, and identify overpayments to the contractors. The Coopers and Lybrand staff tasked to do reconciliations are drawn from the same pool of employees that conduct audits or provide management consulting services to Coopers and Lybrand's clients.

Discussion

The performance of the follow-on contract will require that Coopers and Lybrand review contracts with thousands of large and small private-sector firms that may employ their firm to perform audit or consulting services. The existence of this relationship represents a potential conflict of interest because Coopers and Lybrand is unable to render totally impartial assistance or advice.

Federal and DoD regulations provide guidance on conflict of interest. Federal Acquisition Regulation (FAR) 9.505, requires that contracting officers examine each contracting situation to prevent conflicting roles that might bias a contractor's judgment. OMB Policy Letter 89-1, "Conflict of Interest Policies Applicable to Consultants," November 13, 1989, states that prior to contract award, contracting officers will take appropriate steps to identify and evaluate the potential for conflicts of interest, which could be prejudicial to the interest of the United States with regard to persons who provide advisory and assistance services to the Government and take steps to avoid any conflicts believed to exist.

DLA did not determine whether a potential conflict of interest existed with Coopers and Lybrand performing the reconciliations under either the initial contract or the follow-on contract. We believe this action occurred because the contracting officers and sponsoring office for the contract were not cognizant of the relationship that Coopers and Lybrand might have with DoD contractors. We believe that DLA should modify the follow-on contract with Coopers and Lybrand to exclude contracts with the firm's audit clients from those that it reconciles. The contracts that are not reconciled by Coopers and Lybrand can be reconciled by DLA personnel. Modifying the contract to exclude Coopers and Lybrand clients would mitigate any conflict of interest that exists.

Office of Management and Budget (OMB) Circular A-120, "Guidelines for the Use of Advisory and Assistance Services," and DoD Directive 4205.2 define CAAS and provide guidance on the use of CAAS. The Circular defines CAAS to include management and professional support services, which may apply to "management support or related systems including . . . accounting, auditing, and records management." DoD Directive 4205.2, "Contracted Advisory and Assistance Services," implements the Circular. The Directive requires that each DoD Component establish a CAAS Director who is responsible for reviewing and approving all CAAS procurements. The FY 1990 DoD Appropriations Act included a limitation on the amount that DoD could obligate and expend during FY 1990 for CAAS, and prescribed that the DoD must report all contract obligations for CAAS for each quarter of FY 1990 to the Congress and to the Comptroller General.

DLA did not consider the reconciliation services to be CAAS and did not plan to include the follow-on contract in DoD's quarterly report to Congress. The DLA CAAS Director stated that the contracted services were for cleanup of DLA records and therefore were not management support services as defined in the CAAS directives. We do not agree with the Director's rationale and believe the reconciliation services are in the management

support services category of CAAS. Nonreporting of the reconciliation services as CAAS will result in an understatement of DoD's expenditures for CAAS reported to Congress.

Recommendations

We recommend that the Director, Defense Logistics Agency:

1. Modify contract DLA600-90-D-5047 to preclude Coopers and Lybrand from reconciling DoD contracts with Coopers and Lybrand clients.

2. Report contract DLA600-90-D-5047 as contracted advisory and assistance services in accordance with the FY 1990 Department of Defense Appropriations Act.

Management Comments

A draft of this quick-reaction report was provided to the Director, Defense Logistics Agency for comment on May 21, 1990. We received comments from the Deputy Comptroller, Defense Logistics Agency on June 14, 1990. The complete comments are provided at Enclosure 1.

The Deputy Comptroller concurred with Recommendation 1. and stated that the contracting officer had informed the contracting officer's technical representative in writing that Coopers and Lybrand should not reconcile contracts between the Government and its clients. In addition, the contracting officer also advised Coopers and Lybrand on May 29, 1990, that their auditors must not review or reconcile contracts of clients for which they also perform audit or management consulting services. DLA will review those contracts.

The Deputy Comptroller also concurred with Recommendation 2. and stated that contract DLA600-90-D-5047 will be reported as CAAS in the next quarterly report to the Office of the Secretary of Defense. The monetary status of the contract will be reported in subsequent reports during the life of the contract.

Audit Response to Management Comments

We consider DLA's comments on the report to be fully responsive and in conformance with the provisions of DoD Directive 7650.3. Accordingly, additional comments on the final report are not required.

If you have any questions on this audit, please contact Mr. Garold Stephenson on (202) 694-6275 (AUTOVON 224-6275) or Ms. Kim Caprio on (202) 694-3463 (AUTOVON 224-3463). The audit

team members are listed in Enclosure 3. Copies of this report are being provided to the activities listed in Enclosure 4.

The cooperation and courtesies extended to the audit staff are appreciated.



Edward R. Jones
Deputy Assistant Inspector General
for Auditing

Enclosures

cc: Director for Contracted Advisory
and Assistance Services, DoD



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



13 JUN 1990

IN REPLY DLA-CI
REFER TO

MEMORANDUM FOR ACTING DIRECTOR, CONTRACT MANAGEMENT DIRECTORATE,
DEPARTMENT OF DEFENSE, INSPECTOR GENERAL

SUBJECT. Draft Quick-Reaction Report on the Audit of the
Procurement of Contract Reconciliation Services by the
Defense Logistics Agency (Project No. OCH-0040.01)

This is in response to your memorandum, undated, requesting
comments on the quick-reaction report on the Audit of the
Procurement of Contract Reconciliation Services by the Defense
Logistics Agency. The enclosed remarks have been approved by
Helen T. McCoy, Deputy Comptroller, Defense Logistics Agency.

3 Encls

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

TYPE OF REPORT: AUDIT

DATE OF POSITION: 12 Jun 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Quick-Reaction Report on the Audit of the Procurement of Contract Reconciliation Services by the Defense Logistics Agency (Project No. OCH-0040.01)

FINDING: In April 1989, DLA issued a sole-source letter contract (DLAHOO-89-D-0010) to Network Solutions, Inc. (NSI) through the Small Business Administration 8(a) program. The contract was for NSI to provide automatic data processing and telecommunication support for the transition of finance and accounting operations from nine Defense Contract Administration Service Regions (DCASRs) to the Defense Finance Center in Columbus, Ohio. In August 1989, DLA issued Task Order No. 6 to NSI to reconcile over 4,000 selected contracts for transfer from DCASR, Los Angeles, California. NSI subsequently subcontracted with Coopers and Lybrand to reconcile the contracts. Work under the original contract with NSI and Coopers and Lybrand is largely complete. The total value of the contract with NSI is about \$24.6 million, of which approximately \$4.4 million is attributable to contract reconciliation work.

On April 6, 1990, DLA awarded a follow-on contract (DLA600-90-D-5047) to Coopers and Lybrand to reconcile contracts at the other eight DCASRs. The estimated total value of this contract is \$15.0 million.

The contracts to be reconciled are with private-sector firms that provide goods and services to the DoD. The reconciliation process requires that Coopers and Lybrand's staff review contract modifications, contractor invoices, payment vouchers and other documents, validate the disbursements and obligations on the contracts, and identify overpayments to the contractors. The Coopers and Lybrand staff, tasked to do reconciliations, are drawn from the same pool of employees that conduct audits or provide management consulting services to contractor clients.

DLA COMMENTS: Concur. Appropriate measures have been taken by the Contracting Office to preclude review or reconciliation by Coopers and Lybrand of contracts of clients for which they also perform audit or management consulting services.

MONETARY BENEFITS: N/A
DLA COMMENTS:
ESTIMATED REALIZATION DATE:
AMOUNT REALIZED:
DATE BENEFITS REALIZED:

ACTION OFFICER: Dolores Stocks, DMPPMO

DLA APPROVAL: Helen T. McCoy

FORMAT 2 OF 3

TYPE OF REPORT: AUDIT

DATE OF POSITION: 12 Jun 90

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO.: Draft Quick-Reaction Report on the Audit of the Procurement of Contract Reconciliation Services by the Defense Logistics Agency (Project No. OCH-0040.01)

RECOMMENDATION 1: We recommend that the Director, Defense Logistics Agency modify contract DLA600-90-D-5047 to preclude Coopers and Lybrand from reconciling contracts with its contractor clients.

DLA COMMENTS: Concur. The Contracting Office has already taken action to place this requirement directly with the responsible Contracting Officer's Technical Representative (COTR). The applicable statement appears in the COTR's appointment letter in conjunction with other specific guidance and cautionary information pertaining to COTR's responsibilities and performance. The COTR has attested to his understanding of his responsibilities and adherence to all requirements by signing the appointment letter. The letter is part of the Contracting Office's official files. In addition to the appointment letter clause, the contract has been modified by letter to Coopers and Lybrand, advising them that their auditors must not review or reconcile contracts of clients for which they also perform audit or management consulting services. DLA will be responsible for reviewing those contracts in which Coopers and Lybrand have clients.

DISPOSITION:

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

MONETARY BENEFITS: N/A

DLA COMMENTS:

ESTIMATED REALIZATION DATE:

AMOUNT REALIZED:

DATE BENEFITS REALIZED:

ACTION OFFICER: Dolores Stocks, DMPPMO

DLA APPROVAL: Helen T. McCoy

ACTIVITIES VISITED OR CONTACTED

Defense Contract Administration Services Region-Los Angeles, CA
Defense Finance Center, Columbus, OH
Defense Logistics Agency Automated Information Processing Center,
Columbus, OH
Defense Logistics Agency Headquarters, Cameron Station,
Alexandria, VA
Coopers and Lybrand - Arlington, VA
Network Solutions, Inc. - Herndon, VA
Small Business Administration, Office of the Regional Inspector
General, Arlington, VA
Small Business Administration - Washington District Office,
Washington, DC

AUDIT TEAM MEMBERS

David K. Steensma, Director, Contract Management Directorate
James J. McHale, Deputy Director
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Lawrence F. Zaletel, Team Leader
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FINAL REPORT DISTRIBUTION

Office of the Secretary of Defense

Office of the Under Secretary of Defense for Acquisition

Other Defense Activities

Defense Logistics Agency

Non-DoD

Office of Management and Budget
U.S. General Accounting Office,
NSIAD Technical Information Center

Congressional Committees:

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