



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
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ARLINGTON, VIRGINIA 22202-2884

REPORT
NO. 90-108

September 18, 1990

MEMORANDUM FOR DIRECTOR, DEFENSE LOGISTICS AGENCY
COMMANDER, DEFENSE CONTRACT MANAGEMENT
REGION, DALLAS

SUBJECT: Final Report on the Audit of the Administration of the
Contract Closeout Process at the Defense Contract
Management Region, Dallas (Project No. 9AC-0021.03)

Introduction

This is our final report on the Audit of the Administration of the Contract Closeout Process at the Defense Contract Management Region, Dallas (DCMR, Dallas), for your information and use. The work covered by this report is part of our larger audit of the Defense Logistics Agency's contract closeout process. That audit is, in turn, a part of a related Government-wide audit sponsored by the President's Council on Integrity and Efficiency. The audit was made from January to October 1989. The objectives of the audit were to determine the timeliness of the contract closeout process, the validity of unliquidated obligations on contracts awaiting closeout, and the timeliness of collection of overpayments on incentive contracts with cost underruns. As part of the audit, we also evaluated internal controls over the contract closeout process. As of December 31, 1988, the Contract Administration Report at DCMR, Dallas, showed that administrative contracting officers (ACO's) were administering 34,696 contracts and that 5,345 of those contracts were complete and awaiting contract closeout. The contracts that were awaiting closeout had \$117.6 million of unliquidated obligations.

The audit showed that, overall, the Defense Contract Management Region, Dallas, administered the contract closeout process effectively. The Defense Contract Management Region took actions during the audit to advise contracting officers of opportunities to deobligate funds and to take steps to recoup one overpayment. This report contains no recommendations.

Scope of Audit

To accomplish our audit objectives, we randomly selected and reviewed multiple samples of contracts from the Contract Administration Report dated December 31, 1988. Specifically, we selected 56 active contracts, 46 physically complete contracts,

41 dormant contracts, and 43 pay adjustment contracts. In total we selected 186 contracts with unliquidated obligation values totaling \$1.1 billion. The 56 active contracts were selected in order to assess the reliability of the Contract Administration Report. We determined whether contracts reported as active were physically complete and whether they should be included in the closeout process. There were no significant instances of incorrect reporting in the Defense Contract Management Region, Dallas, Contract Administration Report.

Our assessment of the internal controls related to the contract closeout process included an examination of the documentation that support management's implementation of the "Federal Managers Financial Integrity Act," and Office of Management and Budget Circular A-123. We deemed that the internal controls applicable to the contract closeout process were effective, since the audit disclosed no material deficiencies.

This program results audit included an examination and review of ACO contract files and accounting records dated from June 1976 through October 1989. The audit was made in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. Accordingly, we included such tests of the internal controls as were considered necessary. A list of activities visited or contacted during the audit is in Enclosure 2.

Background

The DCMR, Dallas, is one of nine Defense Contract Management Regions within the Defense Logistics Agency that provides contract administration services to DoD, and to other agencies and departments of the Federal Government. DCMR, Dallas, uses an automated information system entitled "Mechanization of Contract Administration Services" (MOCAS), to manage the contract administration process, which includes contract closeout. Briefly, basic contract information (contract numbers, obligations, delivery dates, etc.) is entered into MOCAS when a contract is received at DCMR, Dallas, for administration. The system provides for updating the initial contract information to reflect modifications, deliveries, and numerous other actions that occur during contract performance.

The Contract Administration Report (the Report) is one element of the MOCAS system that provides ACO's with status information for each contract administered. The Report is organized into five sections. Section 1 contains active contracts on which delivery and acceptance of supplies, performance of services, or periods of performance have not been completed. Section 2 contains physically complete contracts on which delivery of supplies and services are completed and

accepted, but contract administration is still pending. Section 3 contains dormant contracts on which one or more of the following are pending: complete terminations for convenience, public law claims, investigations, bankruptcy, litigation, final payments withheld contingent on extended testing after shipment, and contingent value engineering payments. Section 4 of the Report contains contracts that have been closed and reopened by the finance office for payment adjustments. Section 5 contains contracts that have been closed during the month.

Federal Acquisition Regulation (FAR) 4.804, "Closeout of contract files," specifies contract closeout procedures and prescribes time frames for closing contracts that are physically complete. Firm-fixed-price contracts should be closed within 6 months of completion. Contracts requiring the settlement of overhead rates should be closed in 36 months, and all other contract types should be closed in 20 months.

Prior Audit Coverage

Since 1986, the Air Force Audit Agency, the Defense Logistics Agency, and the U.S. Army Audit Agency, have issued a total of four audit reports on the administration of the contract closeout process in DoD. Problem areas identified in the prior audit reports included untimely contract closeout, untimely deobligation of excess funds, and delays in recovery of overpayments.

Discussion

Overall, our audit disclosed that the administration of the contract closeout process at DCMR, Dallas, was generally effective. The integrity of information available for use by ACO's was sufficient for decision making. The strength of internal controls related to the contract closeout process was sufficiently complete and accurate to effectively monitor the timeliness of contract closing, determine the validity of unliquidated obligations, and initiate recovery of refunds due the Government for cost underruns on incentive contracts.

Timeliness of the Closeout Process. To determine whether contracts were closed within the time frames prescribed by the FAR, we determined how long it took to close 130 contracts after the contracts were physically completed. The 130 contracts included 46 contracts in section 2 (physically complete) of the Contract Administration Report, 41 contracts in section 3 (dormant), and 43 contracts in section 4 (payment adjustments).

Our tests disclosed that contracts at DCMR, Dallas, were generally closed within the time frames prescribed by the FAR. Of the 46 physically complete contracts that we reviewed, 38 contracts (83 percent) had not exceeded the time frames

prescribed in the FAR for closing physically completed contracts. The other eight contracts were overage because they were awaiting audits of the final invoices or overhead rates by the Defense Contract Audit Agency, awaiting a submission of overhead rates and final invoices by the contractor, or awaiting funds reconciliation. We also reviewed 41 dormant contracts and 43 pay adjustment contracts. Overall, the contracts were not assigned to sections 3 and 4 for excessive periods of time. We did not assess the timeliness of 27 dormant contracts because they involved bankruptcy or were in litigation. Of the remaining 14 dormant contracts, 10 (71 percent) were not awaiting closeout for excessive periods of time.

Our review of the 43 pay adjustment contracts disclosed that DCMR, Dallas, complied with Defense Logistics Agency Manual 7000.1, "Accounting and Finance Manual," and assigned only contracts to section 4 that had been closed and reopened for payment adjustments. In addition, 38 (88 percent) of the 43 contracts were not awaiting closeout for excessive periods of time.

Validity of Unliquidated Obligations. To determine whether ACO's were recommending that the Services deobligate excess funds on physically complete and dormant contracts, we reviewed 33 contracts that had \$24.7 million of unliquidated obligations. ACO's did not make fund reviews on 11 of the 33 contracts. Six of the eleven contracts did not have excess funds that could be recommended for deobligation. The remaining five contracts had \$6.6 million of unliquidated obligations that the ACO's had not recommended for deobligation. Officials at DCMR, Dallas, agreed that excess funds existed on the contracts and scheduled them for fund reviews.

Management's review of the funds on the five contracts resulted in a recommendation to the procuring contracting officers to deobligate \$1.1 million of excess funds. In addition, DCMR, Dallas, officials issued a memorandum that explained the ACO's responsibility to perform excess fund reviews on completed contracts (see Enclosure 1).

Refunds Due on Incentive Contracts. We reviewed five incentive contracts in our audit sample of physically complete contracts to determine whether ACO's at DCMR, Dallas, had collected overpayments on incentive contracts with cost underruns. Our audit disclosed that one of the five contracts was overpaid by \$15,908 at the time the contract was physically complete. Although the ACO agreed there was a potential overpayment on the contract, the demand for repayment had not been initiated because the procuring official had not negotiated the final price. Officials at DCMR, Dallas, agreed to take appropriate steps to collect any overpayment once the procuring official negotiated the final price of the contract.

Due to actions taken by management during the course of our audit, no recommendations are presented in this report. Since there are no unresolved issues, written comments to this report are not required from you.

The cooperation and courtesies extended to the audit staff are appreciated. Please contact Mr. Salvatore D. Guli, Program Director, at (202) 694-6285 (AUTOVON 223-6285) or Ms. Linda A. Pierce, Project Manager at (202) 693-0560 (AUTOVON 223-0560), if you have any questions. A list of the audit team members is in Enclosure 3. Copies of this report are being provided to the activities listed in Enclosure 4.



Edward R. Jones
Deputy Assistant Inspector General
for Auditing

Enclosures

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



DEFENSE LOGISTICS AGENCY
DEFENSE CONTRACT ADMINISTRATION SERVICES REGION, DALLAS
1200 MAIN STREET, 6TH FLOOR
DALLAS, TEXAS 75202-4399



IN REPLY
REFER TO DCASR DAL-A

28 MAR 1989

SUBJECT: Contract Closeout, Release of Excess Funds

TO: Commanders of DCASMs/DCASPROs
ATTN: Chief, Contract Management Division

1. A recent DoD IG audit survey of the contract closeout process at DCASR Dallas found several instances in which excess funds had not been released in a timely manner on Fixed Price Incentive (FPI) contracts. The general procedures for ACO determination and handling of excess contract funds are outlined in paragraphs 32.7-5d, e, and f of DLAM 8105.1.

2. The ACO should determine whether excess funds are available for release on an FPI contract as soon as possible after it is physically complete, i.e., after delivery of all supplies and/or completion of all services. The availability of excess funds can often be ascertained prior to receipt of the contractor's FPI final settlement proposal. When excess funds are identified, the ACO should immediately notify the PCO and/or process the deobligating supplemental agreement, if/as authorized. However, in no instance, shall the ACO delay such action until completion of the audit review of the FPI final settlement proposal. Also, per paragraph "f" of the aforementioned DLAM reference, it should be noted that these procedures apply to any contract situation in which funds eligible for deobligation can be identified--not just FPI contracts.

3. In view of the audit finding, ACOs must perform an excess funds review immediately on all physically complete contracts in CAR Sections 1, 2, and 3. If any contracts are found to have a significant amount of excess funds, the ACO will follow the DLAM procedures for PCO notification and/or ACO deobligation. In the future, such excess funds review must be made on a quarterly basis to preclude another recurrence of this problem.

4. If additional information is needed on this matter, the POC is Carl Welton, DCASR DAL-AC at AV 940-1346.

FOR THE COMMANDER:


for JAY L. GRAHAM
Director, Contract Management
Directorate

ENCLOSURE 1

ACTIVITIES VISITED OR CONTACTED

Office of the Secretary of Defense

Assistant Secretary of Defense (Production and Logistics),
Washington, DC
Comptroller of the Department of Defense, Washington, DC

Defense Agencies

Defense Logistics Agency, Alexandria, VA
Defense Contract Management Region, Dallas, TX
Defense Contract Management Area Operations:
Dallas, TX
San Antonio, TX
Phoenix, AZ
Defense Plant Representative Offices:
E Systems, Incorporated, Greenville, TX
Rockwell International, Richardson, TX
Texas Instruments, Incorporated, Dallas, TX

AUDIT TEAM MEMBERS

David K. Steensma, Director, Contract Management Directorate
Salvatore D. Guli, Program Director, Contract Administration
Linda A. Pierce, Project Manager
Rayburn H. Stricklin, Project Manager
Michael T. Hill, Team Leader
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Thomas Smith, Auditor
R. Steven Silverstein, Auditor
Beth A. Kilborn, Auditor
Billy J. McCain, Auditor
Leron A. Mims, Auditor

FINAL REPORT DISTRIBUTION

Office of the Secretary of Defense

Assistant Secretary of Defense (Production and Logistics)
Assistant Secretary of Defense (Public Affairs)
Comptroller of the Department of Defense
Deputy Assistant Secretary of Defense (Procurement)

Department of the Army

Secretary of the Army
Assistant Secretary of the Army (Financial Management)
Army (DAIG-PA)

Department of the Navy

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

Department of the Air Force

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

Defense Activities

Director, Defense Contract Audit Agency
Director, Defense Logistics Agency
Commander, Defense Contract Management Region, Dallas

Non-DoD Activities

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

Congressional Committees:

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

