

Audit



Report

OFFICE OF THE INSPECTOR GENERAL

**DOCUMENTATION OF REIMBURSABLE FOREIGN
MILITARY SALES TRANSACTIONS**

Report Number 93-034

December 17, 1992

Department of Defense

The following acronyms are used in this report.

ALC..... Air Logistics Center
CDM.....Contractual Depot Maintenance
CPAS.....Contract Procurement Accounting System
DDRE.....Defense Distribution Region East
DFAS.....Defense Finance and Accounting Service
DLA.....Defense Logistics Agency
FMS.....Foreign Military Sales
ICP.....Inventory Control Point
NSC.....Naval Supply Center
PMS.....Production Management Specialist
ROD.....Report of Discrepancy



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

December 17, 1992

MEMORANDUM FOR COMPTROLLER OF THE DEPARTMENT OF DEFENSE
ASSISTANT SECRETARY OF THE NAVY (FINANCIAL
MANAGEMENT)
ASSISTANT SECRETARY OF THE AIR FORCE (FINANCIAL
MANAGEMENT AND COMPTROLLER)
INSPECTOR GENERAL, DEPARTMENT OF THE ARMY
DIRECTOR, DEFENSE SECURITY ASSISTANCE AGENCY
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Audit Report on Documentation of Reimbursable
Foreign Military Sales Transactions
(Report No. 93-034)

We are providing this final report for your information and use. The report addresses the issue of whether adequate documentation was maintained to support reimbursable foreign military sales transactions. Comments on a draft of this report were received from the Assistant Secretary of the Army (Financial Management) and the Director, Defense Logistics Agency, and were considered in preparing the final report. Comments on the draft were not received from the Navy or the Air Force.

DoD Directive 7650.3 requires that all audit recommendations be resolved promptly. Therefore, the Navy, the Air Force, and the Defense Logistics Agency are requested to comment on the final report by February 16, 1993. Those comments must indicate concurrence or nonconcurrence with the recommendations in Part II. DoD Directive 7650.3 also requires that you comment on the estimated monetary benefits, state the amounts you concur or nonconcur with, and give the reason for your nonconcurrence. Recommendations and potential monetary benefits are subject to resolution in accordance with DoD Directive 7650.3 in the event of nonconcurrence or failure to comment. See the "Status of Recommendations" section at the end of each finding for the recommendations you must comment on and the specific requirements for your comments.

The courtesies extended to the audit staff are appreciated. If you have any questions about this audit, please contact Mr. Alvin L. Madison at (703) 614-1681 (DSN 224-1681) or Mr. Ronald C. Tarlaian at (703) 614-1365 (DSN 224-1365). Appendix F lists the distribution of this report.



Robert J. Lieberman
Assistant Inspector General
for Auditing

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

Office of the Inspector General, DoD

AUDIT REPORT NO. 93-034
(Project No. 2FA-0002)

December 17, 1992

**DOCUMENTATION OF REIMBURSABLE
FOREIGN MILITARY SALES TRANSACTIONS**

EXECUTIVE SUMMARY

Introduction. Reimbursable foreign military sales (FMS) transactions are expenditures for which the U.S. Government has made a monetary investment in the sale before the FMS customer makes payment. Reimbursable transactions include stock issues from DoD inventories and contractual depot maintenance expenditures for the repair and return of Defense articles. From October 1, 1986, to September 30, 1991, 3,711 FMS cases had reimbursable transactions amounting to \$2.7 billion. We reviewed 187 high-dollar value FMS cases that had reimbursable transactions valued at \$640.1 million.

Objectives. The objectives of the audit were:

- o to determine whether reimbursable FMS transactions reported by the Military Departments were adequately supported, documented, and recorded so that the transactions could be used to verify reported expenditures and subsequent customer billings; and

- o to evaluate internal controls over FMS reimbursable transactions billed to FMS customers.

Audit Results. The Military Departments did not properly bill and support reimbursable transactions billed to FMS customers, resulting in overcharges of about \$1.2 million and undercharges of \$4 million. Also, Military Departments did not maintain documentation for \$55.4 million in customer billings.

- o Military Departments did not accurately bill and document stock issues from DoD inventories in accordance with DoD regulations. Further, the Army and the Air Force lacked effective internal controls to ensure that items shipped to FMS customers were accurately billed. As a result, FMS customers were overcharged \$1.1 million on two cases and undercharged \$740,000 on four cases. Military Departments also could not support customer billings of \$41.9 million (**Finding A**).

- o Air Logistics Centers (ALCs) had not established reconciliation procedures to ensure that expenditures for contractual depot maintenance were accurately billed to FMS customers. The ALCs did not comply with DoD regulations by maintaining documentation to support each charge. As a result, FMS customers were overcharged by \$54,000 on two cases and

undercharged \$3.3 million on nine cases. The ALCs also could not support customer billings of \$13.5 million, and the ALCs may have to absorb unsupported costs if customers make claims of discrepancies (**Finding B**).

Internal Controls. This report identifies two material internal control weaknesses. First, the Army and the Air Force did not have effective internal control procedures to ensure that Defense articles shipped to FMS customers were accurately billed. Also, the Air Force had ineffective reconciliation procedures to ensure that contractual depot maintenance expenditures were accurately billed to FMS customers. See Findings A and B for details of these weaknesses. A description of the controls assessed is on page 2 of Part I.

Potential Benefits of Audit. This report identifies net monetary benefits of \$2.8 million from the recoupment of reimbursable expenditures not billed to foreign military sales customers. Appendix D summarizes the monetary and nonmonetary benefits.

Summary of Recommendations. We recommended that the Military Departments and the Defense Logistics Agency comply with DoD regulations by maintaining supporting documentation for reimbursable transactions from case initiation to case closure. We also recommended that the Air Force Materiel Command require the Air Logistics Centers to establish procedures to ensure that all contractual depot maintenance expenditures are accurately billed to FMS customers.

Management Comments. The Army concurred in part with Recommendation A.2. and concurred with Recommendation A.3. The Army's comments satisfy the intent of the recommendations. Defense Logistics Agency nonconcurred with Recommendation A.3. The Navy and the Air Force provided no comments to be included in this report. Comments on the final report are required from the Navy, the Air Force, and the Defense Logistics Agency by February 16, 1993. See Part II for a full discussion of management comments and Part IV for the complete texts of management comments.

TABLE OF CONTENTS

	Page
TRANSMITTAL MEMORANDUM	
EXECUTIVE SUMMARY	i
PART I - INTRODUCTION	1
Background	1
Objectives	1
Scope	1
Internal Controls	2
Prior Audits and Other Reviews	3
PART II - FINDINGS AND RECOMMENDATIONS	5
A. Billing and Documenting Sales of Inventory Items	5
B. Contractual Depot Maintenance Transactions	11
PART III - ADDITIONAL INFORMATION	15
APPENDIX A - Reimbursable Cases and Case Selections	17
APPENDIX B - Erroneous Billings for Sales from DoD Inventories	19
APPENDIX C - Billing Discrepancies for Contractual Depot Maintenance Transactions	21
APPENDIX D - Summary of Potential Benefits Resulting from the Audit	23
APPENDIX E - Activities Visited or Contacted	25
APPENDIX F - Report Distribution	27
PART IV - MANAGEMENT COMMENTS	29
Department of the Army	31
Defense Logistics Agency	35

This report was prepared by the Financial Management Directorate, Office of the Assistant Inspector General for Auditing, DoD. Copies of the report can be obtained from the Secondary Reports Distribution Unit, Audit Planning and Technical Support Directorate (703) 614-6303 (DSN 224-6303).

PART I: INTRODUCTION

Background

Definition. Reimbursable foreign military sales (FMS) transactions are expenditures for which the U.S. Government has a monetary investment in the sale before the FMS customer makes payment. Reimbursable transactions include stock issues from DoD inventories and contractual depot maintenance expenditures for the repair and return of Defense articles for FMS customers.

Governing regulations. DoD Manual 7290.3-M, "Foreign Military Sales Financial Management Manual," states that all reimbursable transactions must be documented and that documentation must be maintained in case files from case implementation until case closure. Military Departments and the Defense Logistics Agency (DLA) designate the activities that will be responsible for certain parts of cases and the documents to be maintained in case files. Designated activities are required to maintain documents until final billing statements are issued to FMS customers. DoD Manual 7220.9-M, "DoD Accounting Manual," explains the process that the Military Departments must follow to ensure that all costs are properly reimbursed.

Objectives

The objective of this audit was to determine whether reimbursable transactions reported for FMS by the Military Departments were adequately supported, documented, and recorded so that expenditures could be verified and properly billed. We also evaluated the internal controls over reimbursable transactions billed to FMS customers.

Scope

Sample selection process. We obtained reports from the Military Departments that listed all reimbursable transactions billed to FMS customers from October 1, 1986, through September 30, 1991. The reports listed 3,711 cases with an estimated delivered value of \$2.7 billion. From these reports, we selected 187 FMS cases with a delivered value of \$640.1 million, based on a delivered value of at least \$100,000 per case. We reviewed 100 Army cases: 40 cases at the U.S. Army Tank Automotive Command; 30 at the U.S. Army Armament, Munitions, and Chemical Command; and 30 at the U.S. Army Missile Command. For the Naval Air Systems Command, we reviewed 40 cases at 5 Naval Supply Centers and 6 activities of the Naval Industrial Fund. We also reviewed 47 Air Force cases: 10 cases at Ogden Air Logistics Center (ALC), 10 at San Antonio ALC, 9 at Warner Robins ALC, and 18 that involved all three ALCs. Appendix A lists the reimbursable cases by major activity.

Elements of scope. We obtained Letters of Offer and Acceptance and other relevant information from case files. We also obtained financial requisition histories showing the amount expended for each reimbursable transaction. For each case reviewed, we determined the type of reimbursable transaction and the amount billed to the FMS customer. We reviewed all documentation in case files (item release/receipt documents, shipment planning worksheets, and financial records) to ensure that FMS customers were accurately billed and bills were properly documented. We also reviewed the procedures and systems that each activity used to maintain shipping documentation and record reimbursable expenditures.

Audit period, locations, and standards. This economy and efficiency audit was made from September 1991 through May 1992 in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD, and accordingly included such tests of internal controls as were considered necessary. Appendix E lists the activities we visited or contacted.

Internal Controls

Controls assessed. We evaluated the Military Departments' internal control procedures in three areas:

- o maintaining documentation at supply depots for stock issued from DoD inventories;
- o billing and documenting expenditures associated with reimbursable FMS transactions for contractual maintenance; and
- o ensuring that the Military Departments were accurately reimbursed for each transaction.

We also assessed the internal control procedures that Air Force finance and accounting offices used for billing contractual depot maintenance expenditures (costs) to FMS customers.

Internal control weaknesses. We identified material weaknesses as defined by Public Law 97-255, Office of Management and Budget Circular A-123, and DoD Directive 5010.38. The Army and the Air Force did not have effective internal control procedures to ensure that items were correctly shipped and accurately billed to FMS customers. The Air Force also lacked effective reconciliation procedures to ensure that contractual depot maintenance expenditures billed to FMS customers were accurate. The internal control weaknesses are discussed in Findings A and B, together with recommendations to correct the weaknesses. All recommendations, if implemented, will correct the weaknesses. We have determined that net monetary benefits of \$2.8 million can be realized by implementing the recommendations. Copies of this report will be provided to the senior Military

Department officials responsible for internal controls for their use in preparing annual internal control statements.

Prior Audits and Other Reviews

Inspector General, DoD, Report No. 89-099, "Audit of Royal Saudi Foreign Military Sales Case SR-P-GAS," August 18, 1989, identified \$22.8 million in reimbursable transactions for which the Navy did not maintain adequate supporting documentation. As a result, the Navy might have to absorb the cost of \$22.8 million of goods and services provided to Saudi Arabia for which supporting documentation was not maintained. The report contained no recommendations.

PART II: FINDINGS AND RECOMMENDATIONS

A. BILLING AND DOCUMENTING SALES OF INVENTORY ITEMS

The Military Departments did not adequately bill and document the sales of Defense articles from DoD inventories to foreign military sales (FMS) customers. This condition occurred because the Army and the Air Force did not have effective internal control procedures to ensure that Defense articles shipped to FMS customers were accurately billed. Also, the Military Departments did not comply with DoD's requirement to maintain supporting documentation for FMS cases until they were closed. As a result, FMS customers were overcharged \$1.1 million on two cases and undercharged \$740,000 on four cases for the sale of Defense articles. Also, the Military Departments had not maintained documentation to support billings of \$41.9 million; if customers make claims of shipping discrepancies, the Military Departments will have to replace Defense articles or reimburse the customers at Government expense.

DISCUSSION OF DETAILS

Documentation of FMS case files. DoD Manual 7290.3-M, "Foreign Military Sales Financial Management Manual," requires that complete files on FMS cases be maintained by the activities responsible for actions on the cases. Military Departments are allowed to designate those activities responsible for preparing and maintaining case files. The Manual also requires that files be maintained from case initiation until case closure. This requirement ensures that each case file has a complete audit trail for processed transactions.

Reports of discrepancies. FMS customers have 1 year from receipt of a shipment to submit a report of discrepancy (ROD) to the U.S. Government when a material discrepancy or billing error is identified. From October 1, 1986, through September 30, 1991, the Defense Finance and Accounting Service, Denver Center, processed 141,000 RODs for \$137.3 million in reimbursements to FMS customers. The high volume of RODs emphasizes the need for the Military Departments to properly bill and document all reimbursable transactions in order to verify reported expenditures (costs). Also, because the Military Departments conduct research on RODs after the 1-year period has expired, documents must be maintained so that these reviews can be conducted so that the U.S. Government will not have to pay unjustified customer claims.

Billing and documenting transactions. We reviewed 1,832 reimbursable transactions for Defense articles issued from DoD inventories, valued at \$562.8 million. FMS customers were overcharged \$1.1 million on two cases and undercharged \$740,000 on four cases. Also, the Military Departments did not

maintain documentation for 538 transactions to support \$41.9 million in customer billings.

Army. Army depots are responsible for maintaining documentation for all stock issued from inventory. We reviewed 852 stock transactions, valued at \$357.6 million, at 11 Army depots. Depots did not maintain documentation for 100 transactions to support customer billings of \$11.9 million. For 87 of the 100 transactions, the Army's noncompliance with DoD Manual 7290.3-M occurred because the proper suffix codes, which identify specific shipments, were not available for each document. Without the suffix codes, the automated system at the Defense Distribution Region East (DDRE) (formerly the New Cumberland Army Depot) could not retrieve shipping documents to support customer billings. DDRE personnel were aware of this problem and were correcting it. For the remaining 13 transactions, clerical personnel said that supporting documentation was misfiled and could not be located.

Navy. The Naval Supply Centers (NSCs) are responsible for maintaining documentation to support customer billings for Defense articles shipped from inventory. We reviewed 688 reimbursable transactions, valued at \$17.5 million, at 5 NSCs. NSCs did not maintain documentation for 324 transactions to support \$8.2 million in customer billings. NSCs did not comply with the requirement in DoD Manual 7290.3-M to maintain documentation through FMS case closure because Navy procedures required NSCs to maintain documentation for 2 to 4 years for all shipments, whether to FMS or DoD customers. As discussed in DoD, IG, Report No. 89-099, if FMS customers submit RODs, the Navy will have to reimburse customers for the cost of Defense articles for which billings are undocumented.

Air Force. Air Logistics Centers (ALCs) are responsible for accumulating billing data and documenting the sale of Defense articles shipped to FMS customers. At 3 ALCs, we reviewed 292 transactions with a delivered value of \$187.7 million. FMS customers were overcharged \$1.1 million on two cases and undercharged \$740,000 on four cases. Also, ALCs did not maintain documentation for 114 transactions to support \$21.8 million in customer billings.

Erroneous billings. The ALCs did not have effective internal control procedures to ensure that billing information was accurate. Appendix B shows the activities and billings involved.

The case managers and finance and accounting offices did not verify that all billing information (such as the actual materials shipped, shipment quantities, and unit prices) was accurate so that FMS customers would be correctly billed. For example, on FMS Case TK-D-VAT, the San Antonio ALC prepared a shipping document to send 256 modification kits to Turkey. Upon receipt of the shipping document, the finance and accounting office

processed the billing of \$768,000 to the customer. However, the customer did not receive the correct materials because the ALC shipped the wrong items to Turkey. The case manager and the finance and accounting office did not verify that the shipment was completed, and the customer was billed erroneously. Based on our review of this case, the ALC corrected the erroneous billing.

Documentation for inventory items. For 114 transactions, the ALCs did not maintain documentation to support \$21.8 million in customer billings. The Air Force's non-compliance with DoD Manual 7290.3-M occurred at the Ogden ALC when ammunition was shipped from various Army depots. DoD Manual 4500.32-M, "Military Standard Transportation and Movement Procedures," required the shipping activity (in this case, Army depots) to notify the requesting activity (Ogden ALC) within 24 hours that movement of materials had occurred. For 109 of 114 transactions, Army depots did not report shipments to Ogden ALC to confirm the movement of materials to FMS customers. For Ogden ALC to bill FMS customers for ammunition items shipped from inventory, Ogden ALC had to verify that the items had been shipped from Army depots. However, Ogden ALC could not obtain documentation to support the 109 shipments billed to FMS customers. This could cause problems if customers submit material discrepancy reports in the future. For the remaining five transactions, the ALCs could not provide documentation to support the billings because the documents were misfiled.

Responsibility for supply operations. In March 1992, the Defense Management Report Decision No. 902 transferred responsibility for supply and distribution functions at supply depots from the Military Departments to the Defense Logistics Agency (DLA). DLA will be required to ensure that all supply records are accurate and that documentation for all transactions is maintained according to DoD regulations. The Military Departments will be responsible for shipping ammunition and performing maintenance functions at supply depots.

After DLA assumed responsibility for supply and distribution, DLA officials realized that the Military Departments did not have standardized systems for billing and documenting reimbursable transactions. DLA officials also told us that DoD Manual 7290.3-M does not list the specific documentation that should be maintained in case files. They suggested that DoD Manual 7290.3-M be updated to list records that the Military Departments must maintain to support reimbursable transactions and to state how often these records must be updated. DLA officials stated that updating DoD Manual 7290.3-M to standardize the billing and documenting of reimbursable transactions would make the Military Departments' recordkeeping procedures more uniform.

RECOMMENDATIONS FOR CORRECTIVE ACTION

1. We recommend that the Commander, Air Force Materiel Command, require subordinate commands to implement internal control procedures to ensure that customers are accurately billed for stock items issued from DoD inventories.
2. We recommend that the Commander, Depot System Command, require subordinate commands to adhere to established internal control procedures by reporting materials shipped to foreign military sales customers to the appropriate Air Logistics Center for billing.
3. We recommend that the Commander, Depot System Command; the Commander, Naval Supply Systems Command; the Commander, Air Force Materiel Command; and the Director, Defense Logistics Agency, require subordinate commands to comply with DoD Manual 7290.3-M, "Foreign Military Sales Financial Management Manual," by maintaining documentation for stock issued from DoD inventories for foreign military sales from case initiation to case closure.
4. We recommend that the Commander, Air Force Materiel Command, require subordinate commands to correct the erroneous billings for foreign military sales cases listed in Appendix B.

MANAGEMENT COMMENTS

The Army concurred in part with Recommendation A.2. and concurred with Recommendation A.3. On Recommendation A.2., the Army stated that in the Standard Depot System, shipping status is provided by the shipping activity (depot to the requesting activity). The requesting activity is usually the inventory control point (ICP); however, for single-managed items, the ICP and the material owner are not always the same. For ammunition items specified in the report, the ICP is the Army Armament, Munitions, and Chemical Command (AMCCOM), while the material owner is the Air Force (Ogden Air Logistics Center). According to established procedures, the Army depots will notify the ICP (AMCCOM) and not the Air Force (Ogden) that shipment has occurred. These procedures tend to create problems in notification of shipment to the material owner. To avoid this problem, the Army suggested that either the Standard Depot System be changed to notify the material owner or that the Commodity Command Standard System be modified so that the ICP automatically notifies the owner. Regarding Recommendation A.3., the Army stated that although the depots do not have visibility of FMS case status, the requirement to retain documentation for 10 years is valid. The retention of this documentation allows the ICP and the Army Security Assistance Command to reconcile erroneous billing information with depot shipping information.

The Navy and the Air Force did not respond to the draft report.

The Defense Logistics Agency (DLA) nonconcurred with Recommendation A.3., stating that DoD Manual 7290.3-M requires the Military Departments, not DLA, to maintain detail records at the FMS case level. DLA depots and inventory control points control documentation, transactions, and billing records by document number. DoD Manual 7290.3-M does not require DLA to maintain FMS requisitions, shipments, and billing transactions until case closure. DLA was also concerned that the regulatory guidance concerning FMS documentation was inadequate and inconsistent. The guidance does not specify the type of documentation to be retained nor the activity responsible for retaining the documentation. Finally, DLA stated that DoD Manual 7290.3-M and DoD Manual 5105.38-M, the DoD Military Standard Systems regulations and the Federal Acquisition Regulation (FAR), are not in agreement regarding the length of time documentation should be retained.

AUDIT RESPONSE TO MANAGEMENT COMMENTS

The Army's comments were fully responsive to the recommendations.

We request the Navy and the Air Force provide comments to the final report.

We disagree with DLA's position regarding Recommendation A.3. When DLA assumed the responsibility for the supply and distribution functions at depots from the Military Departments, DLA assumed the requirement to comply with DoD Manual 7290.3-M and retain accurate supply records and documentation for stock issued from DoD inventories. With the diversity of FMS cases and the variety of DoD operations, it is impractical for DoD Manual 7290.3-M to specifically list the types of documents to be retained. Rather, DoD Manual 7290.3-M allows the implementing component to identify what organizational elements will be responsible for retaining specific documentation for each FMS case. DoD Manual 7290.3-M also states that the FMS case files should be a comprehensive record of all relevant correspondence and that documentation should be retained from case initiation to case closure. Further, as the Army accurately stated, shipping information is essential when reconciling erroneous billing information or initiating case closure proceedings. Regarding the inconsistencies among regulatory guidance, DoD Manual 7290.3-M and DoD Manual 5105.38-M are the appropriate FMS guidance, not the FAR. Therefore, we request that DLA reconsider its position on Recommendation A.3. when responding to the final report.

STATUS OF RECOMMENDATIONS

Responses to the final report are required from the addressees shown for the items indicated with an "X" in the chart below.

<u>Number</u>	<u>Addressee</u>	<u>Response Should Cover:</u>			<u>Related Issues*</u>
		<u>Concur or Nonconcur</u>	<u>Proposed Action</u>	<u>Completion Date</u>	
A.1., and A.3.	Assistant Secretary of the Air Force (Financial Management and Comptroller)	X	X	X	IC
A.3.	Assistant Secretary of the Navy (Financial Management)	X	X	X	IC
A.3.	Director, Defense Logistics Agency	X	X	X	IC
A.4.	Assistant Secretary of the Air Force (Financial Management and Comptroller)	X	X	X	M

* IC - material internal control weakness
M - monetary benefits

B. CONTRACTUAL DEPOT MAINTENANCE TRANSACTIONS

The Air Force's Air Logistics Centers (ALCs) did not properly bill and document expenditures to foreign military sales (FMS) customers for contractual depot maintenance (CDM) transactions. This condition occurred because ALCs had not established reconciliation procedures to ensure that all charges billed to FMS customers were accurate. Also, the ALCs did not comply with DoD regulations by maintaining documentation to support the amounts charged. As a result, FMS customers were overcharged \$54,000 on two cases and undercharged \$3.3 million on nine cases. The ALCs also did not maintain documentation to support \$13.5 million in customer billings; the ALCs may have to absorb unsupported costs if customers submit reports of discrepancies.

DISCUSSION OF DETAILS

Definitions and governing regulations. Expenditures are made for CDM transactions when contractors' facilities are used to perform services such as scheduled maintenance or repair and return of Defense articles. DoD Manual 7290.3-M, "Foreign Military Sales Financial Management Manual," states that all expenditures must be clearly documented and that documentation must be maintained through case closure. Air Force Materiel Command Manual 66-225, "Contract Depot Maintenance Production and Cost System User's Manual (G072D)," explains how CDM should be performed using the G072D automated system.

Air Force reimbursable procedures. ALCs are responsible for billing and documenting CDM transactions charged to FMS customers. Production Management Specialists (PMSs) are responsible for ensuring that funds are available; arranging for the purchase of resources required to perform services at contractors' facilities; and establishing, updating, and maintaining G072D system records. At the finance and accounting office, the cost accounting branch uses the information from the G072D system to complete a CDM worksheet. The FMS billing office uses the CDM worksheet to report the completion of CDM services to the Defense Finance and Accounting Service (DFAS), Denver Center, for reimbursement. The Contract Procurement Accounting System (CPAS) provides data on CDM expenditures from DFAS Centers or Air Force paying stations for payments made to contractors. CPAS allows ALCs to validate the costs that finance and accounting offices bill to FMS customers.

Sample selection. We selected transactions from 3 ALCs (Ogden, San Antonio, and Warner Robins) and reviewed 17 CDM cases valued at \$41.2 million. We analyzed billing data and obtained documentation from case files to support all charges that the 3 ALCs billed to FMS customers between October 1, 1986, and September 30, 1991. The ALCs' billing documentation was in order when all records related to the charges (contracts, production reports, and G072D system data) were in agreement.

Billing of reimbursable transactions. PMSs and finance and accounting offices at the ALCs needed to reconcile their records to ensure that all CDM charges billed to FMS customers were accurate. FMS customers were overcharged \$54,000 on two cases and undercharged \$3.3 million on nine cases. The G072D system did not allow access to complete information about specific FMS cases and case lines. The PMS had contract information and other documents that were not available to the finance and accounting office. Due to this lack of information, paying stations paid contractors for CDM expenditures when ALCs had not billed FMS customers for the transactions. For example, for FMS Case EG-D-MCH, Line 001, the PMS's records showed that the contractor had submitted invoices and received payment for \$5.9 million for CDM services. However, the finance and accounting office had billed the FMS customer for only \$4.3 million in reimbursable CDM charges, so the FMS customer was undercharged \$1.6 million. This \$1.6 million undercharge would have been avoided if the PMS had reconciled production records to finance and accounting office billing records.

Documentation of reimbursable transactions. The ALCs did not comply with the requirement in DoD Manual 7290.3-M to maintain documentation in support of each CDM charge billed to FMS customers. This resulted in undocumented billings of \$13.5 million; if FMS customers submit reports of discrepancies, the ALCs may have to replace some items at Government expense. The PMSs rely on contractors' monthly production reports, which give the status of work in progress. These production reports are used to update the G072D system, which gives the finance and accounting offices the information needed to bill FMS customers. However, the final production reports do not always agree with G072D system reports (such as contract visibility lists, which detail costs billed to FMS customers). We believe that other sources, such as receiving reports, are needed to verify the accuracy of the PMSs' reports and production reports.

Material inspection and receiving reports. To adequately document CDM transactions, the ALCs should receive copies of Material Inspection and Receiving Reports (DD Forms 250), which are final proof that the contractor has shipped materials. Although ALCs can request DD Forms 250 from the paying stations, all contracts should require the paying stations to send copies of DD Forms 250 to the appropriate ALC. The ALCs would then have documentation to support charges billed to FMS customers; the documentation could be used to reconcile the PMSs' and the finance and accounting office's records. ALCs would have documentation to support billings if FMS customers question any charges.

RECOMMENDATIONS FOR CORRECTIVE ACTION

1. We recommend that the Commander, Air Force Materiel Command, require subordinate commands to:

a. Establish procedures to require the production management specialists and the finance and accounting offices to make quarterly reconciliations of contractual depot maintenance transactions to ensure that foreign military sales customer billings are accurate.

b. Comply with DoD Manual 7290.3-M, "Foreign Military Sales Financial Management Manual," by implementing procedures to require production management specialists and finance and accounting offices to maintain documentation to support all contractual depot maintenance transactions billed to foreign military sales customers from case initiation through case closure.

c. Correct the billing discrepancies listed in Appendix C.

MANAGEMENT COMMENTS AND AUDIT RESPONSE

The Air Force did not respond to the draft report. Therefore, we request the Air Force respond to the final report.

STATUS OF RECOMMENDATIONS

Responses to the final report are required from the addressee shown for the items indicated with an "X" in the chart below.

<u>Number</u>	<u>Addressee</u>	<u>Response Should Cover:</u>			<u>Related Issues*</u>
		<u>Concur or Nonconcur</u>	<u>Proposed Action</u>	<u>Completion Date</u>	
B.1.a., and B.1.b.	Assistant Secretary of the Air Force (Financial Management and Comptroller)	X	X	X	IC
B.1.c.	Assistant Secretary of the Air Force (Financial Management and Comptroller)	X	X	X	M

* IC - material internal control weakness
M - monetary benefits

PART III: ADDITIONAL INFORMATION

- APPENDIX A: Reimbursable Cases and Case Selections
- APPENDIX B: Erroneous Billings for Sales from DoD Inventories
- APPENDIX C: Billing Discrepancies for Contractual Depot
Maintenance Transactions
- APPENDIX D: Summary of Potential Benefits Resulting from the
Audit
- APPENDIX E: Activities Visited or Contacted
- APPENDIX F: Report Distribution

APPENDIX A: REIMBURSABLE CASES AND CASE SELECTIONS

	<u>Total</u> <u>cases</u>	<u>Dollar</u> <u>value</u> <u>(Millions)</u>	<u>Sample</u> <u>cases</u>	<u>Dollar</u> <u>value</u> <u>(Millions)</u>
<u>Activity</u>				
<u>Army</u>				
Armament, Munitions, and Chemical Command	530	\$ 250.4	30	\$ 66.6
Aviation Systems Command	133	76.1	0	0
Communications-Electronics Command	317	55.8	0	0
Missile Command	174	176.7	30	48.6
Tank Automotive Command	312	619.8	40	242.4
Troop Support Command	<u>117</u>	<u>38.2</u>	<u>0</u>	<u>0</u>
Army total	<u>1,583</u>	<u>\$ 1,217.0</u>	<u>100</u>	<u>\$ 357.6</u>
<u>Navy</u>				
Naval Air Systems Command	<u>1,820</u>	<u>\$ 1,116.9</u>	<u>40</u>	<u>\$ 46.1</u>
<u>Air Force</u>				
Ogden Air Logistics Center	71	\$ 47.8	10	\$ 26.6
Oklahoma City Air Logistics Center	9	2.2	0	0
Sacramento Air Logistics Center	8	5.8	0	0
San Antonio Air Logistics Center	58	45.5	10	25.8
Warner Robins Air Logistics Center	34	37.5	9	10.3
Multiple Air Logistics Center	125	226.7	18	173.7
2750th Air Battalion Wing	<u>3</u>	<u>5.9</u>	<u>0</u>	<u>0</u>
Air Force total	<u>308</u>	<u>\$ 371.4</u>	<u>47</u>	<u>\$ 236.4</u>
Total	<u>3,711</u>	<u>\$ 2,705.3</u>	<u>187</u>	<u>\$ 640.1</u>

APPENDIX B: ERRONEOUS BILLINGS FOR SALES FROM DOD INVENTORIES

<u>Activity</u>	<u>Case</u>	<u>Line</u>	<u>Overcharge</u>	<u>Undercharge</u>
OOALC 1/	SR-D-AJO	001	\$ 0	\$ 681,720
	SR-D-AJV	001/2	<u>0</u>	<u>38,400</u>
SAALC 2/	SZ-D-VAL	001	\$ 0	\$ 6,779
	TK-D-VAT	001	<u>768,000</u>	<u>0</u>
WRALC 3/	EG-D-VBE	001	<u>\$ 314,715</u>	<u>\$ 12,871</u>
Total			<u>\$ 1,082,715</u>	<u>\$ 739,770</u>

- 1/ OOALC - Ogden Air Logistics Center
- 2/ SAALC - San Antonio Air Logistics Center
- 3/ WRALC - Warner Robins Air Logistics Center

**APPENDIX C: BILLING DISCREPANCIES FOR CONTRACTUAL DEPOT
MAINTENANCE TRANSACTIONS**

<u>Activity</u>	<u>Case</u>	<u>Line</u>	<u>Overcharge</u>	<u>Undercharge</u>
OOALC	TK-MCE	002	\$ <u>0</u>	\$ <u>284,709</u>
SAALC	EG-MCU	001	\$ 0	\$ 499,662
	ES-MAK	MAL	0	113
	PK-MED	MEG	<u>0</u>	<u>641,278</u>
WRALC	EG-MCH	001	\$ 0	\$ 1,641,343
	EG-MDE	002	0	11,085
	IS-MCR	001	38,315	7,197
	IS-MCX	002	0	5,893
	SR-MBZ	MCA	<u>15,994</u>	<u>\$ 166,976</u>
Total			\$ <u>54,309</u>	\$ <u>3,258,256</u>

APPENDIX D: SUMMARY OF POTENTIAL BENEFITS RESULTING FROM THE AUDIT

<u>Recommendation reference</u>	<u>Description of benefit</u>	<u>Amount and/or type of benefit</u>
A.1.	Internal controls. Improved internal control procedures will ensure accurate billing of stock issues from DoD inventories to FMS customers.	Nonmonetary.
A.2.	Internal controls. Adherence to internal control procedures will ensure that Army depots promptly report material shipped to FMS customers.	Nonmonetary.
A.3.	Compliance. Retention of documents for stock issued from DoD inventory, from case initiation to case closure, will ensure that case files have complete audit trails.	Nonmonetary.
A.4	Program results. Recovery of reimbursable expenditures not charged to FMS cases.	Funds Put to Better Use. Recoupment by the Air Force of \$.7 million not charged to FMS customers, offset by credit or refund of \$1.1 million for over-charges.
B.1.a.	Internal controls. Quarterly reconciliations of contractual depot maintenance records by production management specialists and finance and accounting offices will ensure that customer billings are accurate.	Nonmonetary.

APPENDIX D: SUMMARY OF POTENTIAL BENEFITS RESULTING FROM THE AUDIT (cont'd)

<u>Recommendation reference</u>	<u>Description of benefit</u>	<u>Amount and/or type of benefit</u>
B.1.b.	Compliance. Retention of documentation to support all contractual depot maintenance expenditures from case initiation to case closure will ensure that FMS customer billings are accurate.	Nonmonetary.
B.1.c	Program results. Recovery of reimbursable expenditures not billed to FMS cases.	Funds Put to Better Use. Recoupment by the Air Force of \$3.3 million in contractual depot maintenance charges not billed to FMS customers, offset by credit or refund of \$54,000 for overcharges.

APPENDIX E: ACTIVITIES VISITED OR CONTACTED

Office of the Secretary of Defense

Comptroller of the Department of Defense

Department of the Army

Deputy Chief of Staff for Logistics, Washington, DC
Army Materiel Command, Arlington, VA
Army Security Assistance Command, New Cumberland, PA
Army Armament, Munitions, and Chemical Command, Rock Island, IL
Army Missile Command, Huntsville, AL
Army Tank Automotive Command, Warren, MI
Anniston Army Depot, Anniston, AL
Letterkenny Army Depot, Chambersburg, PA
Red River Army Depot, Texarkana, TX
Seneca Army Depot, Romulus, NY
Sierra Army Depot, Herlong, CA
Tobyhanna Army Depot, Tobyhanna, PA
Iowa Army Ammunition Plant, Middletown, IA
Milan Army Ammunition Plant, Milan, TN

Department of the Navy

Naval Air Systems Command, Washington, DC
Naval Sea Systems Command, Washington, DC
Naval Supply Systems Command, Washington, DC
Navy International Logistics Control Office, Philadelphia, PA
Naval Air Development Center, Warminster, PA
Naval Air Training Center, Lakehurst, NJ
Naval Aviation Depot, San Diego, CA
Naval Ordnance Station, Indian Head, MD
Naval Supply Center, Charleston, SC
Naval Supply Center, Jacksonville, FL
Naval Supply Center, Norfolk, VA
Naval Supply Center, San Diego, CA
Naval Weapons Center, China Lake, CA
Naval Weapons Station, Seal Beach, CA
Pacific Missile Test Center, Point Mugu, CA

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and
Comptroller), Washington, DC
Air Force Materiel Command, Wright-Patterson Air Force Base, OH
Air Force International Logistics Command, Wright-Patterson Air
Force Base, OH
Ogden Air Logistics Center, Ogden, UT
San Antonio Air Logistics Center, San Antonio, TX
Warner Robins Air Logistics Center, Warner Robins, GA

APPENDIX E: ACTIVITIES VISITED OR CONTACTED (cont'd)

Other Defense Agencies

Defense Logistics Agency, Cameron Station, Alexandria, VA
Defense Security Assistance Agency, Washington, DC
Defense Contract Management District, Atlanta, GA
Defense Contract Management District, Los Angeles, CA
Defense Contract Management District, St. Louis, MO
Defense Distribution Region East, New Cumberland, PA
Defense Distribution Region West, Stockton, CA
Defense Finance and Accounting Service, Columbus, OH
Defense Finance and Accounting Service, Columbus Center,
Albuquerque Office, Albuquerque, NM
Defense Finance and Accounting Service, Denver, CO

APPENDIX F: REPORT DISTRIBUTION

Office of the Secretary of Defense

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

Department of the Army

Secretary of the Army
Assistant Secretary of the Army (Financial Management)
U.S. Army Materiel Command

Department of the Navy

Secretary of the Navy
Assistant Secretary of the Navy (Financial Management)

Department of the Air Force

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

Other Defense Agencies

Director, Defense Logistics Agency
Director, Defense Security Assistance Agency
Director, Defense Finance and Accounting Service

Non-DoD Activities

Office of Management and Budget
U.S. General Accounting Office,
National Security International Affairs Division Technical
Information Center

Chairmen and Ranking Minority Members of the following
Congressional Committees:

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

PART IV: MANAGEMENT COMMENTS

Department of the Army

Defense Logistics Agency

Department of the Army



DEPARTMENT OF THE ARMY
OFFICE OF THE DEPUTY CHIEF OF STAFF FOR LOGISTICS
WASHINGTON, DC 20310-0500



DALO-SAA

Chase
24 November 1992
8 DEC 1992
CHARLES A. CHASE DASA
(FINANCIAL OPERATIONS)

T
MEMORANDUM THRU ASSISTANCE SECRETARY OF THE ARMY (FINANCIAL OPERATIONS
MANAGEMENT)

FOR INSPECTOR GENERAL, DEPARTMENT OF DEFENSE (AUDITING), 400 ARMY
NAVY DRIVE, ARLINGTON, VA 22202-2884

SUBJECT: DODIG, Draft Report, Documentation of Reimbursable
Foreign Military Sales Transactions (Project No. 2FA-0002)

1. Reference subject report.
2. Comments on the subject draft report are at Tab A.

FOR THE DEPUTY CHIEF OF STAFF FOR LOGISTICS:

Frank S. Besson III
FRANK S. BESSON III
Director of Security Assistance

Encl

CF:
ASA(I, L, & E)
SAIG-PA (Mrs. Flanagan)

Mr. Liszewski/50390

DOCUMENTATION OF REIMBURSABLE FOREIGN MILITARY SALES
TRANSACTIONS
PROJECT NO. 2FA-0002

FINDING: A. BILLING AND DOCUMENTING SALES OF INVENTORY ITEMS. The Military Departments did not adequately bill and document the sales of Defense articles from DoD inventories to foreign military sales (FMS customers. This condition occurred because the Army and the Air Force did not have effective internal control procedures to ensure that Defense articles shipped to FMS customers were accurately billed. Also, the Military Departments did not comply with DoD's requirement to maintain supporting documentation for FMS cases until they were closed. As a result, FMS customers were overcharged \$1.1 million on two cases and undercharged \$740,000 on four cases for the sale of Defense articles. Also, the Military Departments had not maintained documentation to support billings of \$41.9 million; if customers make claims of shipping discrepancies, the Military Departments will have to replace Defense articles or reimburse the customers at Government expense.

ADDITIONAL FACTS: None.

RECOMMENDATION A-2. We recommend that the Commander, Depot System Command, require subordinate commands to adhere to established internal control procedures by reporting materials shipped to foreign military sales customers to the appropriate Air Logistics Center of billing.

COMMENT. Concur in part. In the Standard Depot System (SDS), shipment status (materiel release confirmation) is provided by the shipping activity (depot to the requesting activity) (Inventory Control Point (ICP)). In the case of single managed items, the ICP and the material owner are not necessarily the same. If the examples cited in the report are single managed items (the report does not specify), the ICP is the U.S. Army Armament, Munitions and Chemical Command (AMCCOM) while the owner is the Air Force (owner records maintained at Ogden ALC). Army depots, following established procedures, will notify the requesting ICP (AMCCOM) and not the material owner (Air Force). This procedure may, indeed, be a loophole in which notification of the owner may not be made. While we see two possible corrective options: (1) a change to the SDS to notify both the ICP and the owner, or (2) modify the Commodity Command Standard System in order to cause the manager to automatically notify the owner, either option requires HQAMC decision and approval. HQAMC has not yet decided which corrective option to implement. HQAMC will make this decision not later than 1 December 1993.

- RECOMMENDATION A-3. We recommend that the Commander, Depot System Command, the Commander, Naval Supply System Command, the Commander, Air Force Materiel Command; and the Director, Defense Logistics Agency, require subordinate commands to comply with DoD Manual 7290.3-M, "Foreign Military Sales Financial Management Manual", by maintaining documentation for stock issued from DoD inventories for foreign military sales from case initiation to case closure.

COMMENT. Concur. Even though the depots do not have visibility of Foreign Military Sales (FMS) case status, the requirement for them to retain FMS shipping documentation in an active file for two years and retired status for another eight, remains valid. Retention of this data enables the ICP and U.S. Army Security Assistance Command to reconcile erroneous billing information with depot shipping information. DESCOM reemphasized the importance of this function to all depots and depot activities in a memorandum dated 13 Nov 92.

Defense Logistics Agency



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



IN REPLY
REFER TO DLA-CI

16 NOV 1992

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING,
DEPARTMENT OF DEFENSE

SUBJECT: Draft Audit Report on Documentation of Reimbursable
Foreign Military Sales Transactions (Project No. 2FA-0002)

We've enclosed our specific comments on recommendation A.3. in response to your 4 September 1992 request. In addition, the following points should be covered in your final report.

This draft audit report does not respond to DLA's concerns about the inadequacy and inconsistency of regulatory guidance regarding FMS documentation. As you pointed out on page 6 of the draft report, current FMS documentation guidance does not state specifically what type documentation is required and who is responsible for retaining it. There is also a disconnect between the DoD Manuals (DoD 7290.3 and DoD 5105.38), the DoD Military Standard Systems (MILS) regulations and the Federal Acquisition Regulation (FAR) regarding the length of time documentation is to be retained. Additionally, a legal opinion should determine the documentation required to satisfy International Tribunal Requirements.

1 Encl

for A. R. Hendrix
JACQUELINE G. BRYANT
Chief, Internal Review Division
Office of Comptroller

cc:
DLA-CX
DLA-OF
DLA-LR

TYPE OF REPORT: AUDIT DATE OF POSITION: 14 Nov 92

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO: Draft Audit Report on Documentation of Reimbursable Foreign Military Sales Transactions (Project No. 2FA-0002)

RECOMMENDATION A.3 (page 13): We recommend that the Director, Defense Logistics Agency, require subordinate commands to comply with DoD Manual 7290.3-M, "Foreign Military Sales Financial Management Manual," by maintaining documentation for stock issued from DoD inventories for Foreign Military Sales from case initiation to case closure.

DLA COMMENTS: Nonconcur, not applicable to DLA. As defined in DoD Manual 7290.3-M, the Military Services have the responsibility to maintain detail records at the FMS case level. The documentation and transactions at DLA depots, inventory control points, and the detail billing records are controlled by document numbers, not by FMS case numbers. In addition, there is no requirement in DoD Manual 7290.3-M that DLA is maintain FMS requisitions, shipments and billing transactions until case closure.

DISPOSITION:

- Action is ongoing. Estimated Completion Date:
- Action is considered complete.

INTERNAL MANAGEMENT CONTROL WEAKNESSES: Not Applicable to DLA

- Nonconcur. (Rationale must be documented and maintained with your copy of the response.)
- Concur; however, weakness is not considered material. (Rationale must be documented and maintained with your copy of the response.)
- Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

MONETARY BENEFITS: None

DLA COMMENTS: N/A

ESTIMATED REALIZATION DATE: N/A

AMOUNT REALIZED: N/A

DATE BENEFITS REALIZED: N/A

ACTION OFFICER: Jim O'Laughlin, DLA-CX

REVIEW/APPROVAL: Jim O'Laughlin, DLA-CX, x46100, 22 Oct 92

DLA APPROVAL: Helen T. McCoy, Deputy Comptroller

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