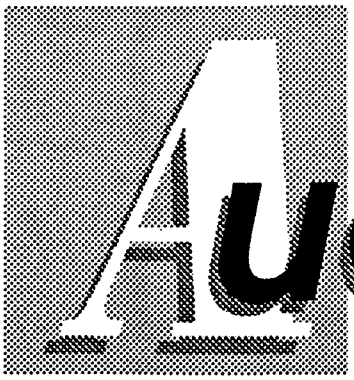

OFFICE OF THE INSPECTOR GENERAL

ACCOUNTS RECEIVABLE FOR DOD MATERIEL

Report No. 94-119 June 3, 1994

Department of Defense

Additional Copies

To obtain additional copies of this report, contact the Secondary Reports Distribution Unit, Audit Planning and Technical Support Directorate, at (703) 614-6303 (DSN 224-6303) or FAX (703) 614-8542.

Suggestions for Future Audits

To suggest ideas for or to request future audits, contact the Planning and Coordination Branch, Audit Planning and Technical Support Directorate, at (703) 614-1868 (DSN 224-1868) or FAX (703) 614-8542. Ideas and requests can also be mailed to:

Inspector General, Department of Defense
OAIG-AUD (ATTN: APTS Audit Suggestions)
400 Army Navy Drive (Room 801)
Arlington, Virginia 22202-2884

DoD Hotline

To report fraud, waste, or abuse, call the DoD Hotline at (800) 424-9098 (DSN 223-5080) or write to the DoD Hotline, The Pentagon, Washington, D.C. 20301-1900. The identity of writers and callers is fully protected.

Acronyms

DFAS	Defense Finance and Accounting Service
DoDAAC	DoD Activity Address Code
SUPSHIP	Supervisor of Shipbuilding, Conversion, and Repair, Newport News

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

June 3, 1994

MEMORANDUM FOR DIRECTOR, DEFENSE PROCUREMENT
ASSISTANT SECRETARY OF THE NAVY (FINANCIAL MANAGEMENT)
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Audit Report on Accounts Receivable for DoD Materiel (Report No. 94-119)

This final audit report is provided for your review and comments. This is the first of two reports from our audit of contractor and agency use of DoD activity address codes. In this report, at Defense Electronics Supply Center request, we address delinquent accounts receivable for materiel purchased from the DoD supply system by contractors. We received management comments from the Director, Defense Procurement, the Navy, and the Defense Logistics Agency on a draft of this report that conformed to DoD Directive 7650.3, and no additional comments from them are required. As a result of management comments, we revised two draft recommendations, added an additional recommendation, deleted one recommendation, and renumbered the other recommendations accordingly.

DoD Directive 7650.3 requires that all recommendations and monetary benefits be resolved promptly. Because the Defense Finance and Accounting Service did not comment on a draft of this report, we request the Director, Defense Finance and Accounting Service, to provide written comments on the final report recommendations and potential monetary benefits by August 2, 1994.

Please contact Mr. Joseph P. Doyle, Program Director, at (703) 692-3218 (DSN 222-3218) or Ms. Linda A. Pierce, Project Manager, at (703) 692-3100 (DSN 222-3100) if you have any questions. We appreciate the courtesies extended to the audit staff. The distribution of this report is listed in Appendix E. The audit team members are listed inside the back cover.

David K. Steensma

David K. Steensma
Deputy Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. 94-119 **June 3, 1994**
(Project No. 3CK-0031)

ACCOUNTS RECEIVABLE FOR DOD MATERIEL

EXECUTIVE SUMMARY

Introduction. As part of our audit of DoD activity address codes, we responded to a Defense Electronics Supply Center, Defense Logistics Agency, request to review overdue accounts receivable for materiel purchased by contractors from the DoD supply system. This report addresses the results of our review of accounts receivable for such contractor materiel purchases.

The December 31, 1993, Defense Finance and Accounting Service monthly management information reports reflected contractor accounts receivable of about $1.8 billion. We could not determine how much of the accounts receivable balance was for materiel purchased by contractors from DoD because the financial data did not separate contractor materiel purchases from other contractor financial transactions.

The Federal Acquisition Regulation permits contractors to obtain materiel from Government sources. The contractors are expected to pay within 30 days of billing or the accounts receivable are considered delinquent and subject to interest charges. We limited our review to $4.6 million of delinquent contractor accounts receivable for materiel purchased by contractors. Some of the $4.6 million was considered delinquent because of accounting errors. We identified the accounts receivable at four Defense Finance and Accounting Service site offices and the Defense Finance and Accounting Service-Columbus Center.

Objectives. The overall audit objective was to evaluate the effectiveness of DoD policies and procedures for authorizing DoD contractors and non-DoD agencies to use DoD activity address codes to obtain materiel from the DoD supply system. The audit included determining whether DoD contractors and non-DoD agencies were properly using DoD activity address codes to obtain materiel from the DoD supply system and the extent to which the DoD Components have fully implemented the management control activity concept. We also evaluated the effectiveness of internal controls and management's implementation of the DoD Internal Management Control Program as they applied to the audit objectives.

This report addresses delinquent contractor accounts receivable for materiel purchased from the DoD supply system. The other objectives will be addressed in a later report.

Audit Results. Four contractors were 19 months to 7 years overdue in paying for materiel obtained from the DoD supply system. The Defense Finance and Accounting Service did not advise authorizing contracting officers or administrative contracting officers of delinquent contractor accounts. Consequently, the Defense Finance and Accounting Service expended extra effort to collect payment or otherwise reconcile the outstanding accounts receivable, yet did not collect or resolve at least $4.6 million of delinquent accounts receivable.

Internal Controls. The audit did not identify any material internal control weaknesses. See Part I for internal controls reviewed.

Potential Benefits of Audit. Of the $4.6 million of delinquent contractor accounts receivable identified, our audit resolved about $1.8 million that should be removed from the accounts receivable records and identified $409,638 for collection. The remaining $2.4 million can be collected or resolved if management implements our recommendations. Coordination among finance officials and contracting officers will reduce the total accounts receivable amounts outstanding and will reduce the administrative burden on the finance offices collecting delinquent accounts receivable. We believe that coordination can and should apply to any accounts receivable, not just those accounts resulting from materiel purchases by contractors, to assist in keeping accounts as current as possible. Appendix C presents the details of the potential benefits of the audit.

Summary of Recommendations. We recommend that contracts state specific terms of purchase for contractors who are permitted to purchase materiel from DoD and that the Defense Finance and Accounting Service notify contracting officers when contractors do not pay for materiel within 30 days of billing. In addition, we recommend that the Navy implement policies that emphasize providing Government-furnished materiel to contractors rather than allow contractors to purchase materiel. We also recommend accounting and collection actions to resolve delinquent accounts receivable for four contractors.

Management Comments. The Director, Defense Procurement, agreed to revise the Defense Federal Acquisition Regulation Supplement and recommended enhancements to the proposed wording. The Navy agreed to issue policy for materiel provided to contractors, and to determine the disposition of discrepant materiel at one contractor facility. The Defense Logistics Agency concurred and stated that the results of the audit clearly indicate problems collecting outstanding contractor payments for materiel purchased from the DoD supply system. The Defense Logistics Agency nonconcurred with our draft recommendation to issue additional policy to affirm Government-furnished materiel as the preferred method of allowing contractors access to the DoD supply system. We did not receive management comments from the Defense Finance and Accounting Service. For a summary of management comments, see Part II. For the complete text of management comments, see Part IV.

Audit Response. We agree with the Director, Defense Procurement, proposed revision to the Defense Federal Acquisition Regulation Supplement wording. We believe that the proposed revisions have strengthened and enhanced the recommendations, and we have incorporated the revisions in the final report. The Navy comments are responsive to the recommendations and we appreciate the actions the Navy has already taken. We accepted the Defense Logistics Agency management comments as responsive and deleted a draft recommendation from the final report. We renumbered the other recommendations accordingly. The Director, Defense Finance and Accounting Service, is requested to provide written comments on the final report recommendations and potential monetary benefits by August 2, 1994.

Table of Contents

Executive Summary i

Part I - Introduction

Background 2
Objectives 3
Scope 3
Methodology 4
Internal Controls 5
Prior Audits and Other Reviews 5

Part II - Finding and Recommendations

Accounts Receivable for DoD Materiel 8

Part III - Additional Information

Appendix A. Criteria for Contractor Access to Government Materiel 22
Appendix B. Status of Accounts Receivable 23
Appendix C. Summary of Potential Benefits Resulting From Audit 24
Appendix D. Organizations Visited or Contacted 27
Appendix E. Report Distribution 29

Part IV - Management Comments

Director, Defense Procurement, Comments 32
Department of the Navy Comments 36
Defense Logistics Agency Comments 38

This report was prepared by the Contract Management Directorate, Office of the Assistant Inspector General for Auditing, DoD.

Part I - Introduction

Background

The Defense Electronics Supply Center, Defense Logistics Agency, requested that we review the amounts due from contractors that purchased materiel from the DoD supply system. We fulfilled their request as part of the audit of contractor and agency use of DoD activity address codes (DoDAACs).

Criteria for Contractor Purchase of Government Materiel. The Federal Acquisition Regulation permits contractors to obtain materiel from Government sources. The procurement contracting officer issues contractors authorization to use Government supply sources to meet contract requirements. Contractors who purchase materiel from DoD are generally expected to pay within 30 days of billing or the accounts receivable are considered delinquent and subject to interest charges. (See Appendix A for specific criteria.)

Materiel Management Within DoD Supply Systems. Inventory control points in each Military Department and the Defense Logistics Agency have primary responsibility for materiel management within DoD supply systems. The military standard requisitioning and issue procedures prescribe procedures for authorized customers, including contractors, to obtain materiel from any DoD Military Department or agency. Each Military Department and agency designates service points to assign DoDAACs. The appropriate service point assigns each customer a DoDAAC based on a request from the authorizing procurement contracting officer. A customer can be assigned more than one DoDAAC. As of September 1993, the DoD activity address file maintained by the Defense Automatic Addressing System Center in Dayton, Ohio, contained about 94,600 DoDAACs for contractors and non-DoD agencies.

DoD Financial Management Consolidation. The Defense Finance and Accounting Service (DFAS) was established in January 1991 to consolidate DoD accounting and finance functions. DFAS is made up of centers, responsible for functional missions, and Defense accounting offices and site offices, responsible for servicing specific locations or organizations. The Defense accounting offices and site offices generally use the finance or comptroller regulations of the Military Department of the activity being served. DFAS is in the process of standardizing the regulations for all DFAS activities.

Administrative Contracting Officer Role. DoD centralized the contract administration mission under the Defense Contract Management Command, Defense Logistics Agency, using administrative contracting officers to perform contract administration functions for most DoD contracts. Administrative contracting officer responsibilities include monitoring contractors' use and control of Government-furnished property, including materiel. The administrative contracting officer generally assigns a property administrator to perform this function. The administrative contracting officer also reviews progress payments to contractors.

Objectives

The overall audit objective was to evaluate the effectiveness of policies and procedures for authorizing DoD contractors and non-DoD agencies to use DoDAACs to obtain materiel from the DoD supply system. The audit included determining whether DoD contractors and non-DoD agencies were properly using DoDAACs to obtain materiel from the DoD supply system and the extent to which the DoD Components have fully implemented the management control activity concept. We also evaluated the effectiveness of internal controls and management's implementation of the DoD Internal Management Control Program as they applied to the audit objectives.

This report addresses delinquent accounts receivable balances for materiel that contractors purchased from the DoD supply system. The audit objectives concerning the Government-furnished materiel process will be addressed in a later report.

Scope

Audit Locations. We selected six inventory control points and their servicing Defense accounting offices or site offices. We included Army, Navy, Air Force, and Defense Logistics Agency activities as follows.

o We selected the Army Tank-Automotive Command to avoid duplication with an ongoing Army Audit Agency project involving Government-furnished materiel at other Army inventory control points.

o We reviewed both Navy inventory control points: the Naval Aviation Supply Office and the Navy Ships Parts Control Center.

o We selected one Air Force inventory control point, the Oklahoma City Air Logistics Center, because of the high volume of requisitions for Government-furnished materiel.

o We included the Defense Electronics Supply Center because they requested we review contractor accounts receivable, and the Defense Industrial Supply Center to expand the scope of coverage in the Defense Logistics Agency.

We also reviewed contractor accounts receivable at the DFAS-Columbus Center, which consolidates contractor accounts receivable for Defense Logistics Agency activities. Our review at the DFAS-Columbus Center included accounts receivable payable to the Defense Construction Supply Center. For a complete list of organizations visited or contacted, see Appendix D.

Accounts Receivable. The DFAS December 31, 1993, monthly management information reports reflected contractor accounts receivable of about

$1.8 billion. The monthly reports consolidate the accounts receivable for all DFAS activities, which includes 5 centers, 199 Defense accounting offices, and 83 site offices. We could not determine how much of the accounts receivable balance was for materiel purchased by contractors from DoD because the financial data did not separate contractor materiel purchases from other contractor financial transactions. We identified $4.6 million of delinquent accounts receivable for contractor materiel purchases from five inventory control points.

Limitation to Scope. We did not review accounts receivable for non-DoD agencies. DFAS is reviewing agency to agency payments for purchases from the DoD supply system.

Methodology

Identification of Delinquent Accounts Receivable. We identified $4.6 million of delinquent accounts receivable for contractor-purchased materiel payable to inventory control points in the Navy and in the Defense Logistics Agency. The Army and Air Force do not allow contractors to purchase materiel from their supply systems.

Navy and Defense Logistics Agency. Navy and Defense Logistics Agency inventory control points permitted contractors to purchase materiel from their supply systems. We identified about $4.6 million of delinquent contractor accounts receivable incurred from January 1986 through September 1993 for materiel purchases at four DFAS site offices servicing inventory control points and at the DFAS-Columbus Center. We selected four high-dollar-value delinquent contractor accounts receivable to determine the status of the accounts, whether the accounts were collectible, and what systemic issues contributed to the delinquency of the accounts. We reviewed only one delinquent contractor account for the Defense Electronics Supply Center because most of their delinquent contractor accounts receivable were comparatively small dollar amounts or were delinquent for less than 60 days. See Appendix B for details of the status of each contractor account reviewed.

Army and Air Force. The Army Tank-Automotive Command and the Oklahoma City Air Logistics Center did not have any delinquent accounts receivable for materiel purchased by contractors because of their policies governing contractor access to the supply system. Before April 1993, the Army Tank-Automotive Command required contractors to pay for materiel purchases when requisitions were submitted. In April 1993, the Army Tank-Automotive Command changed its policy to require Government-furnished materiel issues through contract amendments, thus totally eliminating contractor purchases. The Oklahoma City Air Logistics Center provides contractors with Government-furnished materiel on contracts as opposed to selling materiel to contractors.

Use of Computer-processed Data. The accounts receivable balances provided by DFAS came from computer-processed data. We assessed the reliability of

the data and found errors in the Naval Aviation Supply Office accounts receivable and in one Defense Industrial Supply Center account receivable. Billing errors including data input errors, incorrect DoDAAC and billing address information, and missing paperwork required to close out the account receivable after payment contributed to errors in the data base. We resolved the errors we found in the contractor accounts we reviewed in detail. Because we do not make any projections to the total universe of accounts receivable, we believe the opinions, conclusions, and recommendations in this report are valid. We did not use statistical sampling to conduct this review.

Audit Period and Standards. This economy and efficiency audit was accomplished from March through December 1993. 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. We included such tests of internal controls as were considered necessary. The potential benefits associated with this audit are in Appendix C.

Internal Controls

Internal Controls Reviewed. The internal controls applicable to accounts receivable from contractors for materiel purchased from the DoD supply system were deemed to be effective because no material weaknesses were disclosed. In addition, the FY 1992 Annual Statement of Assurance did not contain issues within the scope of the audit objectives.

Internal Management Control Program Implementation. We reviewed the implementation of the DoD Internal Management Control Program and found that, although accounts receivable was not an assessable unit, debt collection was an assessable unit in the DFAS 5-year internal management control plan. When accounts receivable become overdue, they are reported as delinquent accounts and enter the debt collection process. Because the delinquent accounts receivable that we reviewed were in the collection process and we did not identify any material internal control deficiency, we concluded that implementation of the DoD Internal Management Control Program was adequate within the scope of the audit objectives.

Prior Audits and Other Reviews

Inspector General, DoD, Report No. 92-021, "Debt Collection and Deposit Controls," December 13, 1991, concluded that DoD achieved savings through accelerated collection by implementing the Cash Management Action Plan, a set of initiatives to accelerate the collection and deposit of monies due the Government. However, the DoD Components had not implemented prompt or aggressive collection strategies to pursue delinquent accounts. DoD Components' policies and procedures for collecting delinquent accounts were

not consistent with Federal laws and regulations or with DoD directives and instructions. The likelihood of collecting $553 million of delinquent accounts was impaired. The report estimated that $226.5 million (41 percent) of the delinquent accounts at the end of 1989 were uncollectible and should be written off. The report recommended centralizing debt collection functions and developing uniform debt collection operating procedures. Management generally agreed with the report recommendations and changed applicable regulations to standardize the debt collection process.

Part II - Finding and Recommendations

Accounts Receivable for DoD Materiel

Four contractors obtained materiel from the DoD supply system without paying. Contracting officers were not always aware of outstanding contractor accounts receivable for materiel, and were not involved in collecting the delinquent accounts receivable. In addition, contracts did not always specify terms of purchase for purchasing and paying for DoD materiel. As a result, at least $4.6 million of contractor accounts receivable for materiel purchases were delinquent. More than $400,000 of the $4.6 million was going to be written off. In addition, DFAS expended extra effort to track and to attempt to collect the delinquent amounts.

Contractor Accounts Receivable

Contractors Selected for Review. We selected four contractors with $2.2 million of delinquent accounts receivable for materiel purchased from the Naval Aviation Supply Office, the Navy Ships Parts Control Center, and the Defense Logistics Agency. The four contractors selected were:

o General Electric Company-Aircraft Engines, Lynn, Massachusetts (GE-Lynn);

o General Electric Company-Aircraft Engine Maintenance Center, Strother, Kansas (GE-Strother);

o Rockwell International Corporation, Los Angeles, California (Rockwell); and

o Newport News Shipbuilding and Drydock Company, Newport News, Virginia (Newport News Shipbuilding).

Results of Contractor Review. We identified a total of $409,638 that could be collected from three of the four contractors. The remaining $1.8 million should be removed from the accounts receivable. See Table 1 for a summary of the results of our review of the $2.2 million of delinquent accounts receivable at the four contractors. See Appendix B for additional details.

Table 1. Results of Audit Review of Contractor Accounts Receivable

Contractor	Reviewed Accounts Receivable	Status
GE-Lynn	$ 256,623	Due to DoD (includes $4,470 in administrative fees)
	100,328	Previously paid to DoD
	9,747	Remove from accounts receivable (material already returned to DoD)
GE-Strother	923,100	Remove from accounts receivable (loaned material)
Rockwell	122,499	Due to DoD
	328,559	Remove from accounts receivable (erroneous accounting entry)
Newport News Shipbuilding	30,516	Due to DoD (includes $108 not previously billed)
	127,012	Previously paid to DoD
	102,366	Remove from accounts receivable (materiel was discrepant)
	186,904	Remove from accounts receivable (materiel was returned or not received)
Total Amount Reviewed	$2,187,654	

DFAS was preparing to remove $404,156 of the $2.2 million of accounts receivable we reviewed, without collection, an action commonly referred to as a write-off. Without the audit effort, the $404,156 would have been written off and lost to DoD. The following paragraphs summarize the details of the four contractor accounts receivable we reviewed.

GE-Lynn. DFAS accounts receivable records showed that GE-Lynn owed $274,371 for materiel purchased from the Naval Aviation Supply Office and $87,857 for materiel purchased from the Defense Logistics Agency. The DFAS-Columbus Center made telephone calls and sent at least five formal

written collection notices between January 1992 and July 1993 to try to collect the accounts receivable from GE-Lynn. During that time, the administrative contracting officer was not aware that GE-Lynn owed the money.

Addresses and DoDAACs. The DoD activity address file showed an incorrect address for the GE-Lynn account, therefore, DoD materiel shipments and bills were sent to an incorrect address. Because DoD did not use the correct contractor address, GE-Lynn had difficulty matching bills with shipments and properly routing the bills for payment. Although GE-Lynn provided the inventory control point with proper address information, the DoD activity address file, the central file of DoDAAC addresses maintained for all DoD customers, was not updated. When DoD organizations used the DoDAAC in the requisition process, the incorrect address was automatically used on materiel shipments and billings. We provided GE-Lynn with a point of contact to correct the DoDAAC address information.

Payments and Amounts Due. The DFAS-Columbus Center was preparing to write off a portion of the GE-Lynn accounts receivable. However, we determined that the bills involved were already collected or were still collectible. In total, we identified $252,153 of delinquent accounts receivable that GE-Lynn owed to DoD, and $100,328 that GE-Lynn already paid but that was not credited to the proper accounts. Another $9,747 of materiel was returned to the Government and should have been credited to GE-Lynn's account.

Actions Taken as a Result of Audit. Once notified by the audit team of the delinquent accounts receivable, GE-Lynn initiated action to pay the outstanding account. In addition, the property administrator from Defense Contract Management Area Operations, Boston, Massachusetts, and officials from GE-Lynn took immediate corrective action to implement internal procedures to prevent future bills from going unpaid. We notified the proper DFAS officials of payments already made so that DFAS could adjust the accounts receivable. In September 1993, GE-Lynn paid the amounts due in full, $252,153, plus $4,470 in administrative fees, for a total of $256,624. The previous finance office did not charge interest on delinquent accounts receivable. However, the DFAS site office now servicing the Naval Aviation Supply Office implemented a new accounting system in November 1993 and will charge interest on delinquent accounts as appropriate.

Administrative Contracting Officer Potential to Assist. The administrative contracting officer, if informed of the delinquent account, could have assisted the contractor to identify and correct the problem with the address information in the central DoDAAC file. The administrative contracting officer could also assist DFAS to trace payments already made by the contractor and to collect the amounts due by making contact with the appropriate contractor personnel to track down the paperwork and the materiel or by offsetting the amounts due from progress payments being made to the contractor.

GE-Strother. Accounts receivable at the DFAS site office servicing the Naval Aviation Supply Office were erroneously established to show that GE-Strother owed DoD $923,100 as of January 1993. The account was for

rotor blades that GE-Strother borrowed to support contracts with the Naval Air Systems Command. The Naval Aviation Supply Office item manager and GE-Strother verbally agreed that the contractor would repay DoD with like rotor blades and that GE-Strother would not be assessed interest or any other charges. The administrative contracting officer for GE-Strother was not involved in the arrangement and was unaware of the delinquent account receivable.

DFAS headquarters officials stated that setting up an account receivable in an attempt to track the materiel was not proper accounting. Naval Supply Systems Command officials stated that the inventory records should have been annotated with an appropriate condition code rather than establishing an account receivable. GE-Strother returned the rotor blades to the Government in December 1993.

Rockwell. The accounts receivable records at the DFAS site office servicing the Naval Aviation Supply Office showed that Rockwell owed $358,679 as of June 30, 1993, for materiel purchased from the Naval Aviation Supply Office. According to the DFAS-Columbus Center accounts receivable records, Rockwell owed another $92,379 as of July 23,1993, for materiel purchased from the Defense Logistics Agency. The administrative contracting officer at Rockwell was unaware of the delinquent accounts. As a result of the audit, the administrative contracting officer requested Rockwell to pay the total $451,058 in full or provide documentation that Rockwell does not owe for the materiel. The original bills were dated from April 1989 through November 1991.

We reviewed the Rockwell delinquent accounts receivable with the assistance of the Naval Air Systems Command project manager and determined that bills totaling $328,559 contained an incorrect code in the requisition and that the Government should have been billed for the materiel instead of Rockwell. Therefore, $328,559 of the $451,058 of accounts receivable for Rockwell were accounting errors and should be removed from the Rockwell account. As of March 7, 1994, Rockwell had not paid the remaining $122,499.

Newport News Shipbuilding. As of May 13, 1993, accounts receivable records at the DFAS site office servicing the Navy Ships Parts Control Center showed that Newport News Shipbuilding owed DoD $446,690 for materiel purchased. The bills were outstanding from 1986. The Supervisor of Shipbuilding, Conversion, and Repair, Newport News (SUPSHIP), Virginia, had contract administration responsibilities for Newport News Shipbuilding. With the assistance of personnel from the DFAS site office, SUPSHIP, Navy Ships Parts Control Center, and Newport News Shipbuilding, we determined that of the $446,690 of delinquent accounts receivable, Newport News Shipbuilding owed DoD $30,408, and the remaining $416,282 should be removed from the accounts receivable. We also identified an additional $108 that Newport News Shipbuilding owed for materiel not previously invoiced. As a result of the audit, Newport News Shipbuilding paid the total $30,516 due. The bills to Newport News Shipbuilding clearly stated that interest would be due on late payments. The DFAS site office servicing the Navy Ships Parts Control Center will calculate and bill for any additional interest due.

Bills Already Paid. Newport News Shipbuilding had paid $127,012 of the outstanding accounts receivable before this audit, but the payments were either not identified with the correct bills and invoices or were recent and were not posted to the account. DFAS could not always determine which bill was paid or whether the correct amounts were paid. The DFAS site office servicing the Navy Ships Parts Control Center should adjust the Newport News Shipbuilding accounts receivable to reflect the amounts determined to be previously paid.

Discrepant Materiel. Newport News Shipbuilding was holding materiel valued at $102,366 that did not meet contractual physical specifications. SUPSHIP instructed Newport News Shipbuilding not to return the discrepant materiel to the Navy Supply Center, Norfolk, because other discrepant materiel had been shipped to the Navy Supply Center, Norfolk, on previous occasions and had been lost by the center after receipt. SUPSHIP has plant clearance responsibility for Newport News Shipbuilding and should provide Newport News Shipbuilding with proper disposition instructions for the discrepant materiel. Upon completion of the disposition of the materiel, DFAS can remove the $102,366 from the accounts receivable for Newport New Shipbuilding.

Materiel Not At Newport News Shipbuilding. Newport News Shipbuilding either returned usable materiel to Navy supply centers or SUPSHIP or did not ever receive materiel valued at a total of $186,904. According to SUPSHIP and the Navy Ships Parts Control Center, most of the materiel that Newport News Shipbuilding returned to Navy supply centers was lost by the supply centers after receipt. Materiel that Newport News Shipbuilding turned in to SUPSHIP was sent to the Intra-Fleet Supply Support Operations Team to be returned to the supply system for reuse. According to receiving and inspection reports reviewed at SUPSHIP, some materiel that Newport News Shipbuilding ordered did not arrive at all, or the shipments received contained only partial orders. Over time, accountability was lost.

We believe that the DFAS site office servicing the Navy Ships Parts Control Center should remove the $186,904 from the Newport News Shipbuilding accounts receivable because Newport News Shipbuilding neither used the materiel nor received other compensation for the materiel.

Payment Terms Established. DFAS was unsuccessful in collecting or resolving the $446,690 of outstanding accounts receivable partly because the Navy supply centers were not always able to provide proof that the materiel was shipped to Newport News Shipbuilding. DFAS had difficulty following Newport News Shipbuilding requisition and payment records because Newport News Shipbuilding did not pay for materiel when billed and did not report discrepant materiel or short shipments. As a result, the Navy Ships Parts Control Center requested SUPSHIP to establish specific payment terms and to require Newport News Shipbuilding to report shipments of discrepant materiel. Except for the delinquent bills discussed above, Newport News Shipbuilding has kept its account with the Navy Ships Parts Control Center current since establishing specific payment terms and proper procedures for receiving and

accepting materiel in November 1992. See Table 2 for the status of the entire $446,690 of delinquent accounts receivable and the $108 not previously billed for Newport News Shipbuilding.

Table 2. Status of Accounts Receivable From Newport News Shipbuilding

Status	Amount
Due to DoD, previously billed	$ 30,408
Due to DoD, not previously billed	108
Paid as a result of audit	30,516
Previously paid to DoD	127,012
Discrepant Materiel	102,366
Materiel returned to DoD or not received	186,904

Defense Electronics Supply Center Delinquent Accounts Receivable and Bankruptcies

As of March 31, 1993, the Defense Electronics Supply Center had delinquent accounts receivable due from contractors for materiel totaling about $1,000,000. About $700,000 of these delinquent debts were from active contractors. More than $300,000 was due from contractors that went bankrupt before paying for materiel obtained from the Defense Electronics Supply Center.

Wilderness Electronics, Incorporated, Accounts Receivable. Wilderness Electronics, Incorporated, had the largest delinquent account receivable balance at the Defense Electronics Supply Center, receiving more than $222,000 of materiel before going bankrupt. More than $76,000 of that materiel was obtained after the contract was terminated for default. Wilderness Electronics, Incorporated, was later prosecuted for fraud and is no longer in business. In this case, neither the administrative contracting officer nor the procurement contracting officer were aware that the contractor was not paying for materiel ordered from the Defense Electronics Supply Center. The money was not collected and Wilderness Electronics, Incorporated, was not cut off from the supply system.

If the finance officer had notified the administrative contracting officer as delinquencies occurred, we believe that the administrative contracting officer would have facilitated collection actions. If the finance officer had notified the

procurement contracting officer, we believe that the procurement contracting officer would have cut the contractor off from the supply source before Wilderness Electronics, Incorporated, received $222,000 of materiel without paying for it.

Other Defense Electronics Supply Center Accounts Receivable. We did not review additional accounts receivable in detail at the Defense Electronics Supply Center because of the low dollar value of individual accounts compared to accounts receivable at other inventory control points. We believe, however, that if the Defense Electronics Supply Center implements our recommendations, the collection of accounts receivable from contractors who purchase materiel will improve, regardless of the amount of the purchase.

Accounts Receivable Write-Offs

In 1992, the Naval Aviation Supply Office wrote off about $240,500 of accounts receivable for materiel purchased by contractors. In July 1993, the DFAS-Columbus Center was considering writing off $84,870. From October 1991 through March 1993, the Navy Ships Parts Control Center wrote off about $199,000, and in September 1993, was considering a write-off of $319,286 of the Newport News Shipbuilding accounts receivable. Such write-offs occur year after year and generally represent lost funds to DoD. Write-offs are often the effect of delinquent accounts receivable such as the ones discussed in this report. We believe that if management implements the recommendations in this report, the majority of these losses could be prevented in the future. Early coordination and action by finance and contracting officials and specific terms of purchase and payment in contracts will facilitate the timely collection of accounts receivable and will minimize the cost to finance offices of collecting delinquent accounts receivable.

Potential Monetary Benefits

As a result of the audit, we resolved about $2.2 million of delinquent accounts receivable for materiel purchased from the DoD supply system. This $2.2 million included $409,638 of potential collections from contractors and $1.8 million of accounting adjustments and property actions. An additional $2.4 million of accounts receivable from the inventory control points we visited and the DFAS-Columbus Center may also be collected or otherwise resolved if management implements our recommendations. GE-Lynn will pay $4,470 of administrative fees related to their delinquent accounts receivable. In addition, an undeterminable amount of interest cost on outstanding balances and administrative costs for repeated tracking and follow-up actions on delinquent accounts receivable can be saved. We believe that coordination between finance

and contracting officials will reduce the total amounts outstanding. In addition, prompt collection of accounts due will reduce the administrative burden of the finance offices.

Conclusion

Federal Acquisition Regulation subpart 32.614-1, "Interest Charges," requires that interest charges be assessed when payments are delinquent. We believe that the suspension or termination of a contractor's access to the DoD supply system would serve as another deterrent to taking improper advantage of Government resources. A minor change to the Defense Federal Acquisition Regulation Supplement would protect the Government's interests by requiring that contracts clearly define the payment terms and the consequences of late or non-payment for materiel, which includes charging contractors interest and suspending contractor access to DoD materiel.

We believe contracts must contain specific terms of purchase for purchasing materiel from DoD and for paying for those purchases. In the case of Newport News Shipbuilding, the contractor did not follow DoD receiving and paying procedures. As time passed and the contract administrators did not address the problems, resolution became difficult and ultimately resulted in the Government's consideration to write off the account. The problems with Newport News Shipbuilding abated after specific terms of purchase were established, including materiel receiving and acceptance procedures and payment terms.

We believe that if the DFAS billing and collecting personnel notify administrative contracting officers and procurement contracting officers when accounts receivable for materiel become delinquent, the collection process can be improved. Property administrators in the contract administration office can determine the status of the materiel and administrative contracting officers can assist in obtaining payment from the contractors, including recovering the amounts due from progress payments. In the example with GE-Lynn, we were able to collect more than $250,000 by identifying the delinquent accounts to the administrative contracting officer staff and obtaining their assistance in collecting the accounts from GE-Lynn. Procurement contracting officers can also intervene by withdrawing or suspending a contractor's authorization for access to Government supply sources until delinquent accounts are paid or resolved.

Recommendations, Management Comments, and Audit Response

Revised, Added, Deleted, and Renumbered Recommendations. As a result of management comments, we revised draft Recommendations 1.a. and 1.b., added a new 1.b., and renumbered draft Recommendation 1.b. as 1.c. We deleted draft Recommendation 3. and renumbered the remaining recommendations accordingly.

1. We recommend that the Director, Defense Procurement, Office of the Under Secretary of Defense for Acquisition and Technology, direct the Defense Acquisition Regulations Council to:

a. Add the following paragraph to the Defense Federal Acquisition Regulation Supplement 251.102(e).

> "(6) Use the format in Table 51-1, Authorization to Purchase from Government Supply Sources. Specify the terms of purchase, including contractor acceptance of any Government materiel, payment terms, and the addresses required by paragraph (f) of the clause at 252.251-7000, Ordering from Government Supply Sources."

b. Add 251.105, Payment for Shipments, to the Defense Federal Acquisition Regulation Supplement.

> "Contractor payments for purchases from Government sources are due within 30 days of the date of the Government's invoice."

c. Amend the Defense Federal Acquisition Regulation Supplement 252.251-7000, "Ordering From Government Supply Sources," to add the underlined words to the clause at paragraph (d)(4), and add paragraph (f).

> (d) When placing orders for Government stock, the Contractor shall--
>
> * * * * * * *
>
> (1) - (3) --No change--
>
> (4) Pay <u>invoices from Government supply sources within 30 days of the date of the invoice. For purposes of computing interest for late contractor payments, the Government's invoice is deemed to be a demand for payment in accordance with the Interest clause of this contract. The contractor's failure to pay may also result in the contracting officer terminating the contractor's authorization to use Government supply sources. In the event the contracting officer terminates the authorization, such termination shall not provide the contractor with an excusable delay for failure to perform or complete the contract in accordance with the terms of the contract, and the contractor shall be solely responsible for any increased costs.</u>
>
> * * * * * * *

(e) --No change--

(f) Government invoices shall be submitted to the contractor billing address, and contractor payments shall be sent to the Government remittance address specified below:

Contractor Billing Address (include point of contact and telephone number):

Government Remittance Address (include point of contact and telephone number):

Management Comments. The Director, Defense Procurement, concurred with draft Recommendations 1.a. and 1.b. and proposed alternate and additional wording for the Defense Federal Acquisition Regulation Supplement.

Audit Response. We agree with the revisions proposed by the Director, Defense Procurement, and incorporated the alternate and additional wording in the final report. We added Recommendation 1.b. using the Director, Defense Procurement, wording to clarify the payment terms. We consider the Director, Defense Procurement, comments responsive and an enhancement to the effectiveness of our audit effort. No additional comments are required.

2. We recommend that the Assistant Secretary of the Navy (Research, Development, and Acquisition) issue policy that establishes the issuance of Government-furnished materiel as the preferred method of allowing contractors access to the DoD supply system for materiel.

3. We recommend that the Commander, Naval Sea Systems Command, direct the Supervisor of Shipbuilding, Conversion, and Repair, Newport News, to:

a. Determine the appropriate disposition of $102,366 of discrepant materiel at the Newport News Shipbuilding and Drydock Company.

b. Provide disposition instructions for discrepant materiel to Newport News Shipbuilding and Drydock Company.

c. Notify the Defense Finance and Accounting Service site office at the Navy Ships Parts Control Center of the disposition of the discrepant materiel at Newport News Shipbuilding and Drydock Company.

Management Comments. The Navy concurred with Recommendations 2. and 3. and will have completed all actions by May 31, 1994.

Audit Response. The Navy comments are responsive to the recommendations and we appreciate the Navy's prompt action to issue policy for materiel provided to contractors, and to determine the disposition of discrepant materiel at one contractor.

4. We recommend that the Director, Defense Finance and Accounting Service:

a. Establish procedures requiring finance officers to notify administrative contracting officers and procurement contracting officers when a contractor does not pay for materiel purchased from DoD within the established payment time allowed and to request assistance in obtaining payment.

b. Collect $256,624 due from the General Electric Company-Aircraft Engines, Lynn, Massachusetts.

c. Make the appropriate accounting adjustments to remove $100,328 from the General Electric Company-Aircraft Engines, Lynn, accounts receivable for bills previously paid.

d. Credit the General Electric Company-Aircraft Engines, Lynn, accounts receivable for $9,747 of materiel returned to the Government.

e. Reverse the accounting entry that established the General Electric Company-Aircraft Engine Maintenance Center, Strother, Kansas, $923,100 account receivable for rotor blades on loan.

f. Adjust the accounts receivable for Rockwell International Corporation to reverse the $328,559 of erroneous accounts receivable entries.

g. Collect or otherwise resolve $122,499 of outstanding accounts receivable due to the Naval Aviation Supply Office and the Defense Logistics Agency from Rockwell International Corporation.

h. Collect $30,516 owed to the Navy Ships Parts Control Center by the Newport News Shipbuilding and Drydock Company.

i. Calculate, bill, and collect appropriate interest on $30,408 of delinquent accounts receivable owed to the Navy Ships Parts Control Center by the Newport News Shipbuilding and Drydock Company.

j. Make the appropriate accounting adjustments to remove $127,012 from the Newport News Shipbuilding and Drydock Company accounts receivable for bills previously paid.

k. Use the Supervisor of Shipbuilding, Conversion and Repair, Newport News, property disposition determination referred to in Recommendation 2. to remove the $102,366 from the accounts receivable for discrepant materiel at the Newport News Shipbuilding and Drydock Company.

l. Write off $186,904 of outstanding accounts receivable not owed to the Navy Ships Parts Control Center by the Newport News Shipbuilding and Drydock Company.

Management Comments Required

The Director, Defense Finance and Accounting Service, did not comment on a draft of this report. Therefore, we request final comments on the recommendation directed to the Director, Defense Finance and Accounting Service, by August 2, 1994.

Part III - Additional Information

Appendix A. Criteria for Contractor Access to Government Materiel

The following Government regulations allow contractors access to Government materiel and prescribe payment terms for materiel purchased by contractors.

Access to Government Supply Sources

Federal Acquisition Regulation 51.1, "Contractor Use of Government Supply Sources," authorizes contractors to obtain materiel from Government sources.

Federal Acquisition Regulation 51.102(f), "Authorization to Use Government Supply Sources," states that the authorizing agency shall be responsible for any debts for supplies that are not satisfied by the contractor.

Defense Federal Acquisition Regulation Supplement 251.1, "Contractor Use of Government Supply Sources," establishes a standard format to authorize contractors to purchase materiel from Government sources.

Terms of Purchase and Payment

Federal Acquisition Regulation 32.614-1, "Interest Charges," requires that interest charges be applied to contract debts unpaid after 30 days from the issuance of a demand.

Federal Acquisition Regulation 52.232-17, "Interest," establishes Government rights in the contract to assess interest for delinquent contractor payments.

Defense Federal Acquisition Regulation Supplement 252.251-7000, "Ordering From Government Supply Sources," establishes the contract terms for contractors purchasing materiel from Government supply sources.

DoD 7220.9-M, DoD Accounting Manual, chapter 24, "Installation-Level Budgetary Resources," requires payment from contractors before any materiel is issued.

Appendix B. Status of Accounts Receivable

Contractor	Inventory Control Point	Value of Delinquent Accounts Reviewed	Amount Due DoD	Amount Previously Paid DoD	Non-Collectible Account Balances
GE-Lynn	Naval Aviation Supply Office	$ 274,371	$242,647[1]	$ 26,447	$ 9,747[2]
	Defense Industrial Supply Center	87,430	13,976	73,454	
	Defense Construction Supply Center	427		427	
GE-Strother	Naval Aviation Supply Office	923,100			923,100[3]
Rockwell	Naval Aviation Supply Office	358,679	30,120		328,559[4]
	Defense Construction Supply Center	92,379	92,379		
Newport News Shipbuilding	Navy Ships Parts Control Center	446,690	30,516[5]	127,012	289,270[6]
Total		$2,183,076	$409,638	$227,340	$1,550,676

[1]Amount includes $4,470 in administrative fees identified by the DFAS site office servicing the Naval Aviation Supply Office. The $4,470 was not part of the original accounts receivable.

[2]GE-Lynn had returned this materiel to supply. This amount should be written off.

[3]Materiel on loan to GE-Strother was shipped to DoD in December 1993.

[4]Original amount was established in error as an account receivable. An accounting entry is needed to reverse the original entry.

[5]Amount includes $108 for materiel not previously invoiced.

[6]$102,366 of materiel is in Newport News Shipbuilding warehouses. Plant clearance or other property action is needed. $186,904 of materiel had been returned to the Government or was never received by Newport News Shipbuilding. This amount should be written off.

Appendix C. Summary of Potential Benefits Resulting From Audit

Recommendation Reference	Description of Benefit	Amount and/or Type of Benefit
1.	Economy and Efficiency. Establishes contract terms of purchase and payment when contractors purchase materiel from the DoD supply system.	Nonmonetary.
2.	Economy and Efficiency. Establishes policy that requires Government-furnished materiel over contractor purchases of materiel from the DoD supply system.	Nonmonetary.
3.a. and b.	Economy and Efficiency. Provides property disposition for materiel valued at $102,366.	Undeterminable.[1]
3.c.	Economy and Efficiency. Provides information to the DFAS for proper accounting adjustments.	Nonmonetary.
4.a.	Economy and Efficiency. Establishes coordination between Government officials dealing with contractors who purchase materiel from the DoD supply system. Prompt payment by contractors will save the Government the cost of money.	Undeterminable. An amount for the cost of money can not be determined in advance.
4.b.	Economy and Efficiency. Collect delinquent accounts receivable for materiel purchased from the DoD supply system.	Funds put to better use of $256,624 in stock fund accounts 97X4930 and 17X4911.

See footnotes at end of appendix.

Recommendation Reference	Description of Benefit	Amount and/or Type of Benefit
4.c.	Economy and Efficiency. Resolves $100,328 of accounts receivable for bills previously paid. Saves further administrative efforts to collect or resolve the account.	Undeterminable.[2]
4.d.	Economy and Efficiency. Resolves $9,747 of accounts receivable for materiel returned to the Government. Saves further administrative efforts to collect or resolve the account.	Undeterminable.[2]
4.e.	Economy and Efficiency. Resolves erroneous accounts receivable totaling $923,100 for materiel loaned from the DoD supply system.	Nonmonetary.
4.f.	Economy and Efficiency. Corrects the erroneous accounts receivable balance totaling $328,559. Saves further administrative efforts to collect or resolve the account.	Undeterminable.[2]
4.g.	Economy and Efficiency. Collects or resolves accounts receivable due from the contractor for materiel purchased from the DoD supply system.	Funds put to better use of $122,499 in stock fund account 97X4930.
4.h.	Economy and Efficiency. Collects accounts receivable due from the contractor for materiel purchased from the DoD supply system. This money was going to be written off before our audit.	Funds put to better use of $30,516 in stock fund account 97X4930.

See footnotes at end of appendix.

Appendix C. Summary of Potential Benefits Resulting From Audit

Recommendation Reference	Description of Benefit	Amount and/or Type of Benefit
4.i.	Economy and Efficiency. Collects interest on delinquent accounts.	Undeterminable.[3]
4.j.	Economy and Efficiency. Resolves $127,012 of accounts receivable for bills previously paid. Saves further administrative efforts to collect or resolve the account.	Undeterminable.[2]
4.k.	Economy and Efficiency. Resolves delinquent accounts receivable totaling $102,366 through accounting adjustments. Saves further administrative efforts to collect or resolve the account.	Undeterminable.[2]
4.l.	Economy and Efficiency. Resolves delinquent accounts receivable totaling $186,904 through accounting adjustments. Saves further administrative efforts to collect or resolve the account.	Undeterminable.[2]

[1]Amount is subject to results of property disposition determination.
[2]Quantity and value of administrative effort saved can not be determined.
[3]Amount will be determined by DFAS based on interest calculations made in accordance with appropriate regulations.

Appendix D. Organizations Visited or Contacted

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition and Technology, Washington, DC
Comptroller of the Department of Defense, Washington, DC
Director, Defense Procurement, Washington, DC
Director, Defense Acquisition Regulations Council, Arlington, VA

Department of the Army

Assistant Secretary of the Army (Research, Development, and Acquisition), Washington, DC
Office of the Deputy Chief of Staff for Logistics, Washington, DC
Army Materiel Command, Alexandria, VA
  Tank-Automotive Command, Warren, MI
Army Audit Agency, Alexandria, VA

Department of the Navy

Office of the Comptroller, Washington, DC
Naval Air Systems Command, Arlington, VA
Naval Sea Systems Command, Arlington, VA
  Supervisor of Shipbuilding, Conversion, and Repair, Newport News, VA
Naval Supply Systems Command, Arlington, VA
  Naval Aviation Supply Office, Philadelphia, PA
  Navy Ships Parts Control Center, Mechanicsburg, PA

Department of the Air Force

Office of the Deputy Assistant Secretary of the Air Force (Contracting), Washington, DC
Air Force Materiel Command, Wright-Patterson Air Force Base, OH
  Ogden Air Logistics Center, Hill Air Force Base, UT
  Oklahoma City Air Logistics Center, Tinker Air Force Base, OK
Office of Special Investigations, McClellan Air Force Base, CA

Defense Organizations

Defense Logistics Agency, Alexandria, VA
- Defense Contract Management Command, Alexandria, VA
  - Defense Contract Management Area Operations
    - Boston, MA
    - El Segundo, CA
    - Wichita, KS
  - Defense Plant Representative Office, General Electric Company - Aircraft Engines, Lynn, MA
- Defense Electronics Supply Center, Dayton, OH
- Defense Industrial Supply Center, Philadelphia, PA
- Defense Fuel Supply Center, Alexandria, VA
- Defense Personnel Support Center, Philadelphia, PA
- Defense Construction Supply Center, Columbus, OH

Defense Finance and Accounting Service, Arlington, VA
- Columbus Center, Columbus, OH
- Site Office, Defense Electronics Supply Center, Dayton, OH
- Site Office, Defense Industrial Supply Center, Philadelphia, PA
- Site Office, Defense Personnel Support Center, Philadelphia, PA
- Site Office, Navy Ships Parts Control Center, Mechanicsburg, PA
- Site Office, Naval Aviation Supply Office, Philadelphia, PA

Defense Contract Audit Agency Resident Office, Boston, MA

Non-Government Organizations

Baxter International, Incorporated, Deerfield, IL
General Electric Company-Aircraft Engines, Lynn, MA
General Electric Company-Aircraft Engine Maintenance Center, Strother, KS
Newport News Shipbuilding and Drydock Company, Newport News, VA
Rockwell International Corporation, Los Angeles, CA

Appendix E. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition and Technology
Comptroller of the Department of Defense
  Deputy Comptroller (Management Systems)
    Director, Management Improvement
  Deputy Comptroller (Program/Budget)
Director, Defense Procurement
Assistant to the Secretary of Defense (Public Affairs)
Director, Defense Acquisition Regulations Council

Department of the Army

Secretary of the Army
Auditor General, Department of the Army

Department of the Navy

Secretary of the Navy
Assistant Secretary of the Navy (Financial Management)
Assistant Secretary of the Navy (Research, Development, and Acquisition)
Comptroller of the Navy
Commander, Naval Air Systems Command
Commander, Naval Sea Systems Command
Commander, Naval Supply Systems Command
Commander, Naval Aviation Supply Office
Commander, Navy Ships Parts Control Center
Commander, Supervisor of Shipbuilding, Conversion, and Repair, Newport News
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)
Auditor General, Air Force Audit Agency

Defense Organizations

Director, Defense Finance and Accounting Service
  Director, Columbus Center
  Director, Site Office, Defense Electronics Supply Center
  Director, Site Office, Defense Industrial Supply Center
  Director, Site Office, Naval Aviation Supply Office
  Director, Site Office, Navy Ships Parts Control Center
Director, Defense Logistics Agency
  Commander, Defense Contract Management Command
    Commander, Defense Contract Management Area Operations, Boston
    Commander, Defense Plant Representative Office, General Electric Company - Aircraft Engines, Lynn
  Commander, Defense Electronics Supply Center
  Commander, Defense Industrial Supply Center
  Director, Defense Logistics Studies Information Exchange
Director, Defense Contract Audit Agency
Inspector General, Central Imagery Office
Inspector General, Defense Intelligence Agency
Inspector General, National Security Agency
Audit and IMC Liaison, National Security Agency

Non-Defense Federal Organizations

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

Chairman and Ranking Minority Member of Each of the Following Congressional Committees and Subcommittees:

  Senate Committee on Appropriations
  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 Subcommittee on Legislation and National Security, Committee on Government Operations

Part IV - Management Comments

Director, Defense Procurement, Comments

Final Report Reference

OFFICE OF THE UNDER SECRETARY OF DEFENSE

3000 DEFENSE PENTAGON
WASHINGTON DC 20301-3000

ACQUISITION AND TECHNOLOGY

MAY 1 1994

DP(DAR)

MEMORANDUM FOR DIRECTOR, CONTRACT MANAGEMENT DIRECTORATE, OFFICE OF THE ASSISTANT INSPECTOR GENERAL FOR AUDITING, DOD

THROUGH: CHIEF, CONGRESSIONAL ACTIONS AND INTERNAL REPORTS 18 May 94

SUBJECT: Accounts Receivable for DoD Material (Project No. 3CK-0031)

This responds to your March 14, 1994, memorandum, requesting comments on recommendations 1.a. and 1.b. in the subject draft audit report.

Revised

Recommendation 1.a. is that DFARS 251.102(e) be revised to add specific language drafted by your office. Recommendation 1.b. is that the clause at DFARS 252.251.7000 be revised to add specific language.

We have no objection to revising the text and clause that you reference; however, we have drafted language that we consider more preferable. Please let us know if our suggested language satisfies your concerns.

I should point out that we currently are planning a total rewrite of the FAR to convert it from rigid rules to guiding principles. We most likely will place a moratorium in the near future on FAR revisions, except those to implement statute or executive order, until after completion of the FAR rewrite. Proposed revisions stemming from this audit report may be affected by that moratorium.

for Eleanor R. Spector
Director, Defense Procurement

Attachment

Final Report Reference

Director of Defense Procurement Comments
Recommendations 1.a. and 1.b.
Draft Audit Report
"Accounts Receivable for DoD Material" (Project No. 3CK-0031)

DoDIG Recommendation 1.a.: Add the following paragraph to DFARS 251.102(e). Revised

> "(6) Shall specify the terms of sale, to include inspection, acceptance, and any unusual payment terms. Payment will normally be due within 30 days of billing, as specified in Clause 252.251-7000, 'Ordering From Government Supply Sources,' unless otherwise specified in the authorization."

DDP Response: We do not object to adding language to DFARS 251.102(e). However, we propose to add the following language:

> "(e) Use the format in Table 51-1, Authorization to Purchase from Government Supply Sources. Specify the terms of the purchase, including contractor acceptance of any Government materiel, payment terms, and the addresses required by paragraph (f) of the clause at 252.251-7000, Ordering from Government Supply Sources."

Use of the term "purchase" rather than "sale" is consistent with language currently in FAR and DFARS Parts 51 and 251. Further, we have included a reference to a new paragraph (f) in the clause at 252.251-7000. Paragraph (f) permits insertion of the addresses to which Government invoices for contractor purchases and contractor payments for such purchases should be sent.

We further recommend adding 251.105, Payment for shipments, as follows: Added as Recommendation 1.b.

> "Contractor payments for purchases from Government sources are due within 30 days of the date of the Government's invoice."

We disagree that the authorization should permit payment in 30 days unless otherwise specified. The standard commercial terms for payment are Net 30 Days and we are concerned that the permissive "unless otherwise authorized" will encourage some contracting officers to either shorten or lengthen this time period beyond the standard commercial practice.

Final Report Reference

Revised and Renumbered as Recommendation 1.c.

DoDIG Recommendation 1.b.: Amend DFARS 252.251-7000, "Ordering From Government Supply Sources," to add the following underlined words to the clause at paragraph (d)(4):

(d) When placing orders for Government stock, the Contractor shall--

* * * * * * * * * *

(4) Pay bills from Government supply sources within 30 days of billing, unless otherwise specified in the letter of authorization. Bills not paid within 30 days of the date due are subject to the interest obligations of the Interest clause in this contract (FAR 52.232-17). Failure to pay bills may result in the suspension or termination of the authorization to obtain materiel from Government sources.

DDP Response: We do not object to revising DFARS 252.251-7000. However, we propose the following revisions:

(d) When placing orders for Government stock, the Contractor shall--

(1) - (3) --No change--

(4) Pay invoices from Government supply sources within 30 days of the date of the invoice. For purposes of computing interest for late contractor payments, the Government's invoice is deemed to be a demand for payment in accordance with the Interest clause of this contract. The Contractor's failure to pay may also result in the Contracting Officer terminating the Contractor's authorization to use Government supply sources. In the event the Contracting Officer terminates the authorization, such termination shall not provide the Contractor with an excusable delay for failure to perform or complete the contract in accordance with the terms of the contract and the Contractor shall be solely responsible for any increased costs.

(e) --No change--

(f) Government invoices shall be submitted to the Contractor Billing Address and Contractor payments shall be sent to the Government Remittance Address specified below:

Contractor Billing Address (include point of contact and telephone number):

Government Remittance Address (include point of contact and telephone number):

(End of clause)

Our proposed language recognizes a standard period of 30 days for contractor payments for purchases from Government sources. This is consistent with standard commercial payment terms of "Net 30 Days." It also clarifies that in computing interest on amounts due to the Government, the Government's invoice for contractor purchases from Government sources constitutes the demand for payment under paragraph (b)(2) of the FAR clause at 52.232-17, Interest. Further, it provides that, if the contractor's authorization to order from Government sources is terminated, any resultant contractor delay or failure to perform, including increased costs of contract performance, are the contractor's responsibility. Lastly, it provides a place in the clause to include addresses where invoices for contractor purchases, as well as where contractor payments for purchases, should be sent.

Department of the Navy Comments

Final Report Reference

THE ASSISTANT SECRETARY OF THE NAVY
(Research, Development and Acquisition)
WASHINGTON, D.C. 20350-1000

6 MAY 1994

MEMORANDUM FOR THE DEPARTMENT OF DEFENSE INSPECTOR GENERAL

Subj: DEPARTMENT OF DEFENSE INSPECTOR GENERAL DRAFT AUDIT REPORT ON ACCOUNTS RECEIVABLE FOR DOD MATERIAL (3CK-0031)

Ref: (a) Department of Defense Inspector General memo of 14 March 94, subject as above

Encl: (1) Department of the Navy Response to Draft Audit Report

I am responding to the draft audit report forwarded by reference (a) concerning delinquent accounts receivable for material purchased from the DoD supply system by contractors.

Draft Recommendation 4. Renumbered as Recommendation 3.

The Department of the Navy concurs with recommendations two and four. Our detailed response to the audit is provided as enclosure (1).

Nora Slatkin

Copy to:
NAVINSGEN
NCB-53

Final Report Reference

DEPARTMENT OF THE NAVY RESPONSE
TO
DODIG DRAFT REPORT OF March 14, 1994
ON
DELINQUENT ACCOUNTS RECEIVABLE FOR MATERIAL
PURCHASED FROM THE DoD SUPPLY SYSTEM BY
CONTRACTORS (3CK-0031)

Finding: Contractors obtained material from the DoD supply system without paying. Contracting officers were not always aware of outstanding contractor accounts receivable for material, and were not involved in collecting the delinquent accounts receivable. In addition, contracts did not always specify terms of sale for purchasing and paying for DoD material. As a result, at least $4.6 million of contractor accounts receivable for material purchases were delinquent. In addition, DFAS expended extra effort to track and attempt to collect the delinquent amounts.

Recommendation 2: Assistant Secretary of the Navy for Research, Development and Acquisition, issue policy that establishes the issuance of Government-furnished material as the preferred method of allowing contractors access to the DoD supply system for material.

Department of the Navy Position: Concur. The Navy will issue a policy memorandum that establishes the issuance of Government-furnished material as the preferred method of allowing contractors access to the DoD supply system for material by 31 May 1994.

Recommendation 4: Commander, Naval Sea Systems Command direct the Supervisor of Shipbuilding, Conversion and Repair, Newport News, to:

Renumbered as Recommendation 3.

a. Determine the appropriate disposition of $102,366 of discrepant materiel at the Newport News Shipbuilding and Drydock Company.

b. Provide disposition instructions for discrepant materiel to Newport News Shipbuilding and Drydock Company.

c. Notify the Defense Finance and Accounting Service site office at the Navy Ships Parts Control Center of the disposition of the discrepant materiel at Newport News Shipbuilding and Drydock Company.

Department of the Navy Position: Concur. SUPSHIP Newport News has determined appropriate disposition of the $102,366 in discrepant materiel. Disposition instructions have been provided to the Newport News Shipbuilding and Drydock Company. The Defense Finance and Accounting Service site office at the Navy Ships Parts Control Center has also been notified of the disposition of the discrepant materiel.

ENCLOSURE( )

Defense Logistics Agency Comments

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

IN REPLY REFER TO DDAI

17 MAY 1994

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING,
DEPARTMENT OF DEFENSE

SUBJECT: Draft Report on Accounts Receivable for DoD Materiel
(Project No. 3CK-0031)

This is in response to your 14 March 1994 request.

2 Encl

JACQUELINE G. BRYANT
Chief, Internal Review Office

cc:
MM
FOX
AQP

TYPE OF REPORT: AUDIT DATE OF POSITION:

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO: Draft Report on Accounts Receivable for DoD Materiel (Project No. 3CK-0031)

FINDING: Accounts Receivable for Materiel. Contractors obtained materiel from the DoD supply system without paying. Contracting officers were not always aware of outstanding contractor accounts receivable for materiel, and were not involved in collecting the delinquent accounts receivable. In addition, contracts did not always specify terms of sale for purchasing and paying for DoD materiel. As result, at least $4.6 million of contractor accounts receivable for materiel purchases were delinquent. In addition, DFAS expended extra effort to track and attempt to collect the delinquent amounts.

DLA COMMENTS:

We concur with the finding. The results of the Inspector General (IG) audit clearly indicate that Department of Defense (DoD) is experiencing problems collecting outstanding contractor payments for materiel purchased from its supply system.

INTERNAL MANAGEMENT CONTROL WEAKNESSES:
( ) Nonconcur.
(X) Concur; however, weakness is not considered material.
( ) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

MONETARY BENEFITS: None Indicated
DLA COMMENTS: None
ESTIMATED REALIZATION DATE: Not Applicable
AMOUNT REALIZED: Not Applicable
DATE BENEFITS REALIZED: Not Applicable

ACTION OFFICER: Darlene DeAngelo, MMSLR, x44012, 5 May 94
REVIEW/APPROVAL: James J. Grady, Jr., Deputy Executive Director, Supply Management, MMSD, x70510, 11 May 94
COORDINATION: FOX, AQP
Anthony Broadnax, DDAI, 11 May 94
[illegible], DDAI, 12 My 94

DLA APPROVAL:

17 MAY 1994

LAWRENCE P. FARRELL, JR.
Major General, USAF
Principal Deputy Director

Final Report Reference

Deleted

TYPE OF REPORT: AUDIT DATE OF POSITION:

PURPOSE OF INPUT: INITIAL POSITION

AUDIT TITLE AND NO: Draft Report on Accounts Receivable for DoD Materiel (Project No. 3CK-0031)

RECOMMENDATION 3. We recommend that the Director, Defense Logistics Agency, issue policy that establishes the issuance of Government-furnished materiel as the preferred method of allowing contractors access to the DoD supply system for materiel.

DLA COMMENTS: We nonconcur with the recommendation. We do not believe that the IG recommendation that Defense Logistics Agency (DLA) issue additional procurement policy is the most expedient solution to the problem. Delinquent DLA accounts receivable for DoD materiel does not appear to be a problem for DLA at the present time. The examples of outstanding claims receivable cited in the draft report were not DLA contracts but Service contracts accessing our Inventory Control Points (ICPs). If Service contracts authorize contractors access to DoD supply systems, we must honor their requisitions.

Under the criteria of Part 51 of the Federal Acquisition Regulation, Use of Government Sources by Contractors, contractor access to the DoD supply sources is already limited to cost-reimbursable contracts which constitute less than .1 percent of DLA's contracting actions. DLA writes fixed-price contracts. ICP access under fixed price contracts constitutes a deviation from accepted policy and requires approval by either Headquarters or the Director of Defense Procurement, depending on whether it is for an individual contracting action or multiple actions.

We recommend this issue be brought to the attention of the Services and resolved at the DoD level. If additional policy in this area is necessary, it would be more appropriate for it to be issued at the DoD level to cover all the military and defense agencies since the problem is not peculiar to DLA.

DISPOSITION:
( ) Action is ongoing. Estimated Completion Date:
(X) Action is considered complete.

INTERNAL MANAGEMENT CONTROL WEAKNESSES:
( ) Nonconcur.
(X) Concur; however, weakness is not considered material.
( ) Concur; weakness is material and will be reported in the DLA Annual Statement of Assurance.

MONETARY BENEFITS: None Indicated
DLA COMMENTS: None
ESTIMATED REALIZATION DATE: Not Applicable
AMOUNT REALIZED: Not Applicable
DATE BENEFITS REALIZED: Not Applicable

ACTION OFFICER: Darlene DeAngelo, MMSLR, x44012, 5 May 94

REVIEW/APPROVAL: James J. Grady, Jr., Executive Director, Supply Management, MMSD, x70510, 11 May 94

COORDINATION: FOX, AQP
Anthony Broadnax, DDAI, x49607, 11 May 94
Bryant, DDAI, 12 May

DLA APPROVAL:

17 MAY 1994

LAWRENCE P. FARRELL, JR.
Major General, USAF
Principal Deputy Director

Audit Team Members

Paul J. Granetto	Director, Contract Management Directorate
Joseph P. Doyle	Audit Program Director
Linda A. Pierce	Audit Project Manager
Beth Kilborn	Senior Auditor
Lawrence Heller	Senior Auditor
Edward Lustberg	Auditor
Lee Anne Hess	Auditor
Donna Starcher	Auditor
Mark Krulikowski	Auditor
Robin Hysmith	Administrative Support