

August 28, 2003



Financial Management

Allegation of Improper
Accounting for Direct Billable
Hours by the Defense Finance
and Accounting Service
(D-2003-127)

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Acronyms

ABS	Automated Billing System
AWC	Automated Workcount
DBH	Direct Billable Hour
DFAS	Defense Finance and Accounting Service
MIPR	Military Interdepartmental Purchase Request
OJCS	Office of the Joint Chiefs of Staff
PBD	Program Budget Decision
RADSS	Resource Analysis Decision Support System
U.S.C.	United States Code
WHS	Washington Headquarters Services



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

August 28, 2003

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE
(COMPTROLLER)/CHIEF FINANCIAL OFFICER
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING
SERVICE
DIRECTOR, WASHINGTON HEADQUARTERS SERVICES
AUDITOR GENERAL, DEPARTMENT OF THE ARMY

SUBJECT: Report on Allegation of Improper Accounting for Direct Billable Hours by
the Defense Finance and Accounting Service (Report No. D-2003-127)

We are providing this report for review and comment. The audit was performed in response to an allegation to the Defense Hotline. We considered management comments on a draft of this report when preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. As a result of management comments, we revised Recommendation B.3. to clarify our intention. Therefore, we request that the Defense Finance and Accounting Service provide additional comments on Recommendation B.3. in response to the final report. We request that management provide the comments by October 27, 2003.

If possible, please provide management comments in electronic format (Adobe Acrobat file only) to Auddfs@dodig.osd.mil. Copies of the management comments must contain the actual signature of the authorizing official. We cannot accept the / Signed / symbol in place of the actual signature. If you arrange to send classified comments electronically, they must be sent over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Questions should be directed to Mr. M. Leon Peek at (703) 604-9587 (DSN 664-9587) or Mr. Carmelo G. Ventimiglia at (317) 510-3852 (DSN 699-3852). See Appendix C for the report distribution. The team members are listed inside the back cover.

By direction of the Deputy Inspector General for
Auditing:

Paul J. Granetto
Director
Defense Financial Auditing
Service

Office of the Inspector General of the Department of Defense

Report No. D-2003-127
(Project No. D2002FI-0108)

August 28, 2003

Allegation of Improper Accounting for Direct Billable Hours by the Defense Finance and Accounting Service

Executive Summary

Who Should Read This Report and Why? This report will be of interest to Defense Finance and Accounting Service (DFAS) personnel who manage the billable hours accounts and DFAS customers who pay for the hours billed. Actions taken as a result of this report could ensure that customers are billed accurately and that changes to data used to generate customer bills are adequately supported.

Background. The audit was initiated in response to an allegation to the Defense Hotline. DFAS operates as a working capital fund entity. As such, DFAS recovers the costs of providing services from the customers it serves. The costs DFAS will incur providing accounting services, measured in direct billable hours, are initially projected as an estimate. The customer then provides funding authority for DFAS to bill for services rendered. Actual hours of labor are recorded and maintained in a database. Hours of labor that exceed the estimate should be billed to the customer. The allegation stated that DFAS management might have directed personnel to significantly reduce the billed amount of direct billable hours reported for accounting services provided to the Army during FY 2001. The allegation cited pressure from upper management to reduce customers' billable hours in order to maintain good customer relations. The allegation also raised the possibility of violations of the Anti-Deficiency Act or other laws. The DFAS Indianapolis Network performed more than 3.8 million in direct billable hours, valued at about \$253 million, during FY 2001.

Results. DFAS Indianapolis Resource Management personnel did not bill the Army for the full cost of the services provided during FY 2001. DFAS Indianapolis Resource Management personnel understated the hours billed by 83,113 hours for the Army and 824 hours for various other customers, thus reducing DFAS FY 2001 collectible revenue by approximately \$5.6 million. When the error was discovered, DFAS Indianapolis Resource Management personnel decided not to bill the customers for the additional revenue owed to DFAS. Also, not all adjustments to the billable hours accounts were properly documented and approved. Formal policies and documented standard operating procedures should help DFAS maintain tighter control over accounting for billable hours. Because the Army has not reimbursed DFAS for the previously unbilled hours, the FY 2003 billing rates for all DFAS Indianapolis customers were higher than they would have been if resource management personnel had collected the \$5.6 million in revenue (see finding A). In our opinion, there was no violation of the Anti-Deficiency Act (see Appendix B).

DFAS revenue was further reduced by \$1.2 million in FYs 2001 and 2002 because services provided to the Office of the Joint Chiefs of Staff during that period were not reimbursed. According to personnel from the Office of the Under Secretary of Defense

(Comptroller)/Chief Financial Officer, funds were to be provided to Washington Headquarters Services according to the Program Budget Decision 416 estimate and should have included amounts for DFAS services to the Office of the Joint Chiefs of Staff. However, neither Washington Headquarters Services, nor the Office of the Joint Chiefs of Staff paid DFAS. As a result, DFAS did not collect approximately \$661,000 in FY 2001 revenue and \$551,000 in FY 2002 revenue. Because DFAS did not receive reimbursement for services provided to the Office of the Joint Chiefs of Staff, FY 2003 billing rates for all DFAS Indianapolis customers were higher than they would have been if resource management personnel had collected the \$1.2 million in revenue. In our opinion, there was no violation of the Anti-Deficiency Act (see finding B).

Management Comments and Audit Response. The Director, Corporate Resources, DFAS concurred with the recommendation that DFAS bill and collect the \$5.5 million from the Army. However, the Director, Finance and Accounting Oversight Directorate, Office of the Assistant Secretary of the Army (Financial Management and Comptroller) nonconcurred with the recommendation to pay DFAS for the accounting services because the funds are being recouped through the FY 2003 billing rates. We agree that the \$5.5 million is being recouped through the FY 2003 billing rates. However, the \$5.5 million is being recouped from all DFAS Indianapolis Network customers, not just the Army. The adjustment that DFAS will make to the FY 2005 billing rates for direct billable hours for the Army and other customers will ensure that the Army, and not other customers, pays for services received by the Army. Also, DFAS concurred with the recommendation to develop and implement written standard operating procedures for the workcount collection and billing process.

The Director, Corporate Resources, DFAS and the Director, Washington Headquarters Services nonconcurred with the recommendation that DFAS bill and collect the \$1.2 million from Washington Headquarters Services for services provided to the Office of the Joint Chiefs of Staff during FYs 2001 and 2002. The Director, Revolving Funds, Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer stated that although she believed Washington Headquarters Services had funds in its budget to support the Office of the Joint Chiefs of Staff, it was not clear from historical budget documents if either agency had funds in their budget to purchase these services. Therefore, it cannot be determined which organization should reimburse DFAS. The Director, Revolving Funds further stated that it was appropriate for DFAS to recoup the loss through changes in FYs 2002 and 2003 rates. We also could not determine which agency should reimburse DFAS. Consequently, we agree it was appropriate for DFAS to recoup the loss through changes in FYs 2002 and 2003 rates.

The Director, Corporate Resources, DFAS nonconcurred with the recommendation that DFAS establish written policy requiring suspension of services by DFAS to customers that do not provide funding in a timely manner. As a result of the DFAS comments, we revised Recommendation B.3. to clarify the intent of the recommendation. A written policy should be developed for addressing issues when customers do not provide funding for services rendered. Suspending services should be an option that can be applied on a case-by-case basis. We request that DFAS consider the revised recommendation and provide additional comments in response to the final report by October 27, 2003. See the Finding section of the report for a discussion of management comments and the Management Comments section of the report for the complete text of the comments.

Table of Contents

Executive Summary	i
Background	1
Objective	3
Findings	
A. Validity of the Allegation	4
B. Unfunded Workcounts	11
Appendixes	
A. Scope and Methodology	18
Prior Coverage	19
B. Allegation and Results	20
C. Report Distribution	21
Management Comments	
Defense Finance and Accounting Service	23
Washington Headquarters Services	26
Department of the Army	27
Under Secretary of Defense (Comptroller)/Chief Financial Officer	28

Background

Allegation. The audit was initiated in response to an allegation referred to the Defense Hotline from the General Accounting Office FraudNet. The complainant alleged that Defense Finance and Accounting Service (DFAS) management might have directed personnel to reduce the billed amount of direct billable hours (DBHs) reported for accounting services provided to the Army by 122,000 hours.

Role of DFAS. DFAS, an entity of the Defense Working Capital Fund, provides financial management services to its customers on a reimbursable or fee-for-service basis. DFAS employs a unit cost methodology to account for the cost of production and develops billing rates for customers. Acceptance of customer orders generates financial resources to replenish working capital and to permit continuing operations. DFAS Indianapolis Resource Management personnel (resource management personnel) are responsible for collecting and reporting DBHs and report to the DFAS Arlington Resource Management Directorate. The client executives for “Operating Forces” and “Sustaining Forces”¹ serve as liaisons between DFAS Indianapolis and its customers. DFAS Indianapolis and its subordinate field accounting sites (the DFAS Indianapolis Network) were the primary providers of accounting services to the Army and various other Defense agency customers during FY 2001.

DFAS Services. The services DFAS provides are categorized into outputs that represent functions such as military and civilian pay, travel pay, debt collection, foreign military sales, and accounting services. In FY 2001, resource management personnel billed DFAS Indianapolis Network customers for 13 different outputs. The output for accounting services is referred to as Output 11 - Direct Billable Hours for Accounting Services. DFAS depends on the workcounts associated with each output for revenue. Accounting services include bookkeeping and preparation of various financial reports, including annual financial statements. The workcount for DBHs is based on direct productive civilian and military labor hours associated with performing accounting services. DFAS also uses workcounts to forecast resources needed to finance future operations and determine future billing rates for each output. The DFAS Indianapolis Network performed more than 3.8 million DBHs, valued at about \$253 million, during FY 2001.

Billing Rates. As a Defense Working Capital Fund entity, DFAS obtains funds to operate by billing its customers for the services it provides. As such, DFAS establishes billing rates that are estimated to recover the cost of providing the services. Once established, billing rates are stabilized for each applicable fiscal year. Stabilized billing rates protect appropriated fund customers from unforeseen cost changes, enabling customers to more accurately plan and budget. Gains or losses in operations may occur as a result of variations in program execution. Realized gains and losses are generally reflected in offsetting adjustments to rates established in subsequent fiscal years. For example, any gains or losses realized in FY 2001 were reflected in the billing rates established for FY 2003. DFAS

¹ In late 2002, Operating Forces and Sustaining Forces were reorganized into one organization, Accounting Services, Army.

established a separate rate for each of the Military Departments and a separate rate for Defense agencies. The FY 2001 DBH billing rates that DFAS established for the Army and Defense agencies were \$66.21 and \$69.56, respectively.

Workcount Collection and Billing. A workcount is a standard unit of measure for a specific output—in this case DBHs of accounting services. During FY 2001, the DFAS Indianapolis Network employees recorded their hours worked in the Automated Time, Attendance, and Production System, which fed into the Resource Analysis Decision Support System (RADSS), the official record of total direct productive hours. Because RADSS did not allocate DBHs to specific customers' accounts, employees used a web-based system, the Direct Billable Hours System, to allocate DBHs to specific customers' accounts. Three to 4 days after the end of each month, resource management personnel compared the total hours recorded in the Direct Billable Hours system to the total direct productive hours recorded in RADSS. The difference between the two totals represented direct hours not assigned to specific customers that resource management personnel proportionally distributed among all customers before entering the DBH workload data in the Automated Workcount (AWC) System, the DFAS agency-wide repository for workcount data. The AWC System electronically transferred the data to the Automated Billing System (ABS) for billing. ABS, a module of the Defense Business Management System, produced the actual customer bills and posted accounting entries to the accounting module of the Defense Business Management System. E-Biz is a new integrated management information system that is scheduled during FY 2003 to replace the workcount collection and billing processes in place during the audit. Finding A contains further information concerning the e-Biz system.

Billing Process. In FY 2001, resource management personnel billed customers mid-month based on estimates for the workload to be performed during the month. Resource management personnel developed the estimates using the previous month's actual data, adjusted for the number of working days in the current month and any known changes expected to occur, such as holidays. Resource management personnel entered the estimates in the AWC System around the 10th of each month. When actual workload data became available the following month, they reversed the estimates, entered the actual data, and prepared revised bills to adjust for differences between the estimates previously billed and the actual workload performed.

United States Code Requirements. Section 2208, title 10, United States Code (10 U.S.C. 2208), states that working capital fund entities, such as DFAS, shall be reimbursed for services rendered. The rates the DFAS Indianapolis Network charges for services provided for an entity should include amounts necessary to recover the full costs of the services provided for that entity. Section 1342, title 31, United States Code (31 U.S.C. 1342), the voluntary services prohibition, provides that an officer or employee of the United States Government may not accept voluntary services or employ personal services exceeding that authorized by law except for emergencies involving the safety of human life. Also, 31 U.S.C. 1301(a), the augmentation provision, prohibits the use of an appropriation for purposes other than those for which the funds were specifically appropriated.

Objective

The objective of our audit was to determine the validity of a Defense Hotline allegation concerning adjustments to DBHs for accounting services provided by DFAS. During the audit, we also noted the DFAS Indianapolis Network was not being reimbursed for accounting services provided to the Office of the Joint Chiefs of Staff (OJCS) and reported the issue in finding B. See Appendix A for a complete discussion of the audit scope and methodology.

A. Validity of the Allegation

The allegation that resource management personnel knowingly understated the number of direct billable hours for accounting services provided to the Army during FY 2001 was valid. DFAS made downward net adjustments of 108,750 DBHs² to FY 2001 billable hours accounts—83,113 DBHs accrued providing services to the Army, and another 824 DBHs accrued for services provided to various other customers. Further, the adjustments made to the billable hours accounts were not always properly approved or documented. The adjustments to the Army and other customers' billable hours accounts were made because DFAS officials did not want to change customer bills to reflect information resource management personnel became aware of at the end of FY 2001. Inadequate documentation of the adjustments, including lack of written approvals, occurred because of a management control weakness evidenced by the absence of documented standard operating procedures for the billing and adjustment process. As a result of making the improper adjustments, resource management personnel did not collect approximately \$5.6 million in revenue, which subsequently caused FY 2003 billing rates for all DFAS Indianapolis Network customers to be higher than they would have been if resource management personnel had collected the \$5.6 million in revenue.

Reductions in Direct Billable Hours

Table 1 identifies the types of adjustments made during FY 2001 by resource management personnel and the associated dollar values of the adjustments.

Table 1. DBH Adjustments for FY 2001		
<u>Adjustment Type</u>	<u>Workcount</u>	<u>Value</u>
Directed Adjustments for:		
Operations and Maintenance, Army	83,113	\$5,502,912
Various Customers	<u>824</u>	<u>57,680</u>
Directed Adjustment Total	83,937	5,560,592
Unbillable Adjustment	<u>24,813</u>	<u>Not Applicable</u>
Total	108,750	\$5,560,592

²This number includes 24,813 hours that were appropriately adjusted because they represent accounting services performed for DFAS. However, this number does not include 287 adjusted hours that, owing to lack of documentation, could not be reconciled to specific customer accounts.

Operations and Maintenance, Army Adjustments. Resource management personnel made downward net adjustments totaling 83,113 hours to the workcount data for the Operations and Maintenance, Army appropriation, one of approximately 20 Army customers purchasing DBHs from the DFAS Indianapolis Network, and the largest of all the DFAS Indianapolis Network customers in FY 2001. Seventy-six percent of DBHs performed by the DFAS Indianapolis Network during FY 2001 related to the Operations and Maintenance, Army appropriation. The downward adjustments resulted in a loss of \$5,502,912 in revenue for the DFAS Indianapolis Network (83,113 DBHs times the Army billing rate of \$66.21 per DBH). In addition, the revenue loss resulted in increased FY 2003 billing rates for all DFAS Indianapolis Network customers. Resource management personnel should bill, and the Army should pay, \$5.5 million for 83,113 DBHs performed in FY 2001 but not billed.

Other Customer Adjustments. Resource management personnel also adjusted downward the accounts of 25 other customers by 824 hours, totaling \$57,680. Five of the 25 other customers' accounts made up 80 percent of the dollars and hours of the adjustments. The \$57,680 is insignificant compared to the \$253 million of total DBHs performed by the DFAS Indianapolis Network during FY 2001. Therefore, we are not recommending that resource management personnel bill the 25 customers for the 824 DBHs.

Unbillable Adjustments. Resource management personnel appropriately removed from the RADSS official DBH total the 24,813 hours of work that the DFAS Indianapolis Network performed for DFAS. These unbilled hours consisted of work performed for bookkeeping and preparation of various financial reports, including annual financial statements and other accounting services. However, resource management personnel did not maintain adequate documentation to support the removal of DBHs for work performed for DFAS. Resource management personnel should continue to remove hours for DBHs performed for DFAS from the RADSS official DBH total, but should maintain adequate documentation to support the DBHs removed.

Reason for Inappropriate Adjustments

Some specific circumstances contributed to the decision to bill customers less than the actual FY 2001 DBH totals. First, resource management personnel experienced problems with an Excel spreadsheet-based tool used to collect DBH data when implementing a new web-based DBH data collection system, the Direct Billable Hours System. Coincidentally, resource management personnel had created a process action team to review the allocation methodology for DBHs not identified to a specific customer. The review resulted in the development of a new methodology. The discovery of the difference between the estimates and the DBHs actually performed was not made until late September 2001, after resource management personnel provided a final year-end bill estimate to the Army in early September 2001. Therefore, DFAS management decided not to bill the Army for actual workcounts that were different than the year-end estimate, and adjusted the DBH totals instead.

Workcount Collection. At the beginning of FY 2001, resource management personnel used an Excel spreadsheet-based tool to collect DBH data. Resource management personnel experienced problems with the spreadsheet-based tool in May 2001 when the new online Direct Billable Hours System was implemented. As a result, for at least 5 months during FY 2001, the AWC System contained only estimates of workcounts because resource management personnel did not have reliable actual workload numbers. In late September 2001, once resource management personnel corrected the problem with the Excel spreadsheet-based tool, they realized that the previously billed estimates were less than the actual hours performed and concluded that the year-end estimate provided to the Army in early September 2001 was understated.

Allocation Methodology. In June 2001, as a result of complaints from Defense agency customers concerning the allocation methodology for DBHs not identified to a specific customer, resource management personnel created a process action team to review the methodology. The team recommended a new methodology for distributing hours to Defense agency customers be implemented retroactive to May 2001. However, resource management personnel did not identify the effect of the team's recommendations until late September 2001.

Decision Not to Bill Additional Hours. Resource management personnel informed us that the Director, DFAS Indianapolis Resource Management, with concurrence from the Operating and Sustaining Forces client executives and the Director, DFAS Arlington Resource Management, directed the downward adjustments of 83,937 DBHs for FY 2001 to account for the 83,937 unbilled hours. Resource management personnel had already provided the Army with a final FY 2001 year-end estimate of \$566 million when they discovered the effect of the problems with the Excel spreadsheet-based tool and the new allocation methodology. Because resource management personnel had already provided the Army with a final year-end estimate, they did not want to go to the Army and request additional funds to cover the understatement of 83,113 DBHs, valued at about \$5.5 million. Resource management personnel made the decision despite the fact that the revised amount was still less than the \$594 million estimate that they had provided the Army at the beginning of FY 2001. Resource management personnel also chose not to bill 25 other customers for 824 unbilled hours.

Soon after the understatement was discovered, resource management personnel should have billed the Army for the 83,113 hours and the 25 other customers for the 824 hours. We believe that it is still important for the Army to pay for the full amount due for accounting services performed during FY 2001. However, due to the relative insignificance of the value of the 824 hours (\$57,680) not billed to various other customers and the potential cost involved with billing and collecting from 25 customers, we are not recommending that resource management personnel bill for the 824 billable hours. In addition, the decision to make 83,937 hours of inappropriate adjustments did not violate the voluntary services provision of the Anti-Deficiency Act (31 U.S.C. 1342). See Appendix B for a more detailed discussion concerning the Anti-Deficiency Act conclusion.

Manual Intervention, Audit Trails, and Standard Operating Procedures

The processes used by resource management personnel to collect and bill for DBHs involved significant manual intervention, lacked adequate audit trails and documentation to support adjustments, and were not documented in written standard operating procedures.

Manual Intervention. Resource management personnel manually intervened in the workcount collection processes when:

- performing the comparison of RADSS and DBH workcount data,
- distributing DBHs not identified to specific customers,
- entering and reversing the monthly accruals in the AWC System,
- uploading the monthly actual data into the AWC System, and
- entering adjustments into the AWC System.

The significant manual intervention subjected the data to a high risk of errors and inaccuracies. DFAS should also ensure that when fully implemented, e-Biz minimizes manual intervention in the DBH collection processes.

Audit Trails. The workcount collection and billing processes also lacked adequate audit trails and documentation to support adjustments. Resource management personnel made the adjustments based on verbal guidance from management, and they did not have readily available documentation to support the adjustments or any written approvals for making the adjustments. Resource management personnel had to search personal files for documents to support the adjustments. The few documents provided to us were difficult to follow and required extensive verbal explanations to enable the auditors to piece together what resource management personnel had done. The lack of adequate audit trails and documentation subjected the data to a high risk of errors and inaccuracies. DFAS should ensure that e-Biz maintains adequate audit trails and documentation for the DBH collection and billing processes.

Standard Operating Procedures. Resource management personnel had not documented the workcount collection and billing processes in standard operating procedures. Newly assigned personnel had to learn the procedures based on verbal explanations or trial and error. Written guidance was not available to assist new personnel in learning their new duties or resolving problems when they occurred. Reductions in resource management staff make it more important than ever that the workcount collection and billing processes be documented to ensure accurate customer bills.

E-Biz Implementation

DFAS will change its process of collecting and distributing DBHs with the implementation of e-Biz. E-Biz is a new, web-based, fully integrated management information system that will integrate the financial management and the time and labor reporting functions. E-Biz will completely replace the billing and workcount collection processes previously described and other DFAS business processes. E-Biz will be implemented in the following four phases:

- Phase I—timekeeping;
- Phase II—budget execution, purchasing, and payables;
- Phase III—project cost accounting, accounts receivable, workcounts, and cost allocation; and
- Phase IV—budget formulation, manpower, and performance measurement.

Resource management personnel anticipate that e-Biz will streamline and automate manual processes, deliver timely and accurate information, and enable a clear understanding of costs. Resource management personnel also stated that, when e-Biz is implemented, manual intervention in the processing of DBHs and customer bills will become the exception rather than the norm. Resource management personnel will have the ability to make manual adjustments in e-Biz. However, if a manual adjustment is made, e-Biz will place the user name on the adjustment and flag the transaction as an adjustment. Also, when e-Biz is fully implemented there will be no proportional distribution of hours to customers; the hours charged by DFAS employees will all be billed directly to customers.

DFAS has already implemented Phases I and II. Phases III and IV were scheduled to be implemented in February and April 2003, respectively. However, on July 31, 2003, we were informed that Phases III and IV had slipped and would be implemented in October 2003. Since Phase III, which includes workcounts, will not begin implementation until October 2003, we were unable to determine whether e-Biz will provide adequate audit trails for DBH data and any changes made to the data. Therefore, DFAS should ensure that standard operating procedures developed for the current process are updated when e-Biz is implemented.

Conclusions

The adjustments resource management personnel made resulted in a revenue loss of approximately \$5.6 million for DFAS. The revenue loss will impact DFAS Indianapolis Network customers through higher than necessary billing rates for FY 2003. To ensure the most equitable recovery of the lost revenue, resource management personnel should bill the Army for the 83,113 DBHs (totaling

\$5.5 million) for accounting services provided during FY 2001. We do not believe resource management personnel need to bill for the 824 unbilled hours because of the cost to bill and collect from the 25 customers and the insignificance of the amount.

DFAS also needs to ensure that e-Biz has adequate audit trails and provides adequate documentation to support adjustments made to the data, and that any adjustments are approved at an appropriate supervisory level. In addition, written standard operating procedures should be developed for the e-Biz process when implemented. If adjustments to customer bills are necessary before the full implementation of e-Biz, resource management personnel need to establish audit trail requirements, documentation requirements, supervisory review requirements and written standard operating procedures for the current workcount collection and billing process.

Recommendations, Management Comments, and Audit Response

A.1. We recommend that the Director, Accounting Services, Army, Defense Finance and Accounting Service Indianapolis:

a. Bill and collect the \$5.5 million from the Army for unbilled direct billable hours for FY 2001.

b. Establish requirements for audit trails, documentation to support adjustments, and supervisory reviews in written standard operating procedures for the workcount collection and billing process. Update the standard operating procedures upon implementation of e-Biz.

Management Comments. The Director, Corporate Resources, DFAS concurred and stated that, based on guidance from the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer, DFAS will adjust the FY 2005 billing rates for DBHs to recoup the portion of the \$5.5 million that was not allocated to the Army in the FY 2003 billing rates. DFAS will also reduce the FY 2005 billing rates for DBHs of those agencies affected by the \$5.5 million loss. In addition, the Director, Corporate Resources concurred with Recommendation A.1.b. and stated that DFAS is developing an agency-wide standard operating procedure that will formalize the currently informal practice of collecting, allocating, and billing DBHs. The standard operating procedure will also specify that appropriate audit trails are maintained to reflect the reasons and justifications for adjustments to customer billings when such adjustments become necessary.

A.2. We recommend that the Assistant Secretary of the Army (Financial Management and Comptroller) pay the \$5.5 million to the Defense Finance and Accounting Service for services provided during FY 2001.

Management Comments. The Director, Finance and Accounting Oversight Directorate, Assistant Secretary of the Army (Financial Management and Comptroller) nonconcurred and stated that the \$5.5 million is being recouped through the FY 2003 billing rates for DBHs.

Audit Response. The Army comments are not responsive. We agree that the \$5.5 million is being recouped through the FY 2003 billing rates. However, the \$5.5 million is being recouped from all DFAS Indianapolis Network customers, not just the Army. The adjustment that DFAS will make to the FY 2005 billing rates for DBHs for both the Army and other customers will ensure that the Army, and not other customers, pay for services received by the Army.

B. Unfunded Workcounts

The DFAS Indianapolis Network provided \$1.2 million in services to the Office of the Joint Chiefs of Staff (OJCS) during FYs 2001 and 2002 without reimbursement. According to personnel from the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer, funds were to be provided to Washington Headquarters Services according to the Program Budget Decision (PBD) 416 estimate and should have included amounts for DFAS services to the Office of the Joint Chiefs of Staff. However, WHS did not provide any funding authority to the DFAS Indianapolis Network on behalf of OJCS due to a disagreement as to who was responsible for the cost of services provided by the DFAS Indianapolis Network to OJCS. As a result, resource management personnel did not collect approximately \$661,000 in FY 2001 revenue and approximately \$551,000 in FY 2002 revenue. The lost revenue caused FY 2003 billing rates for all DFAS Indianapolis Network customers to be higher than they would have been if resource management personnel had collected the funds from WHS to cover the cost of services rendered to OJCS.

Workcount Estimation, Suspension, and Write-Offs

Program Budget Decisions. The annual process for estimating and budgeting for DFAS Indianapolis Network services is embodied, among other places, in the PBD 416, "Defense Financial Operations," and PBD 426, "Cost of Operations and Customer Prices for the Defense Working Capital Funds and Other Revolving Funds." PBD 416 contains estimates of the workload that DFAS Indianapolis Network personnel anticipate performing for each customer, and PBD 426 contains estimates of the cost of services based on the workcount estimate in PBD 416. Each year the Under Secretary of Defense (Comptroller)/Chief Financial Officer approves both PBD 416 and PBD 426. PBD 416 and PBD 426 are designed to forecast workload and rates two years in advance. For example, the PBD 416, dated December 2000, provided workload estimates for FYs 2001 and 2002. PBD 416 specifically states that it is only an estimate, and customers must fund DFAS for the cost of all services provided, which is consistent with guidance in DoD Regulation 7000.14-R, volume 11B, chapter 61, "Progress Billings, Reimbursements, and Revenue Recognition," December 1994.³

Suspended Workcounts. DFAS Indianapolis Network customers normally provide funding for services by using a Military Interdepartmental Purchase Request (MIPR). ABS calculates customer bills based on workcounts and generates a standard form 1080, "Voucher for Transfer Between Appropriations and/or Funds." The ABS billing process (discussed in finding A) is automatic, but ABS cannot generate the transfer until the customer provides a MIPR authorizing the transfer of funds to resource management. ABS automatically

³ DoD Regulation 7000.14-R, volume 11B, chapter 61, "Progress Billings, Reimbursements, and Revenue Recognition," was updated in October 2002 and renumbered as chapter 11.

suspends workcounts if funds are not available for transfer. We identified suspended workcounts, valued at approximately \$1.2 million, for OJCS.

Workcount Write-Offs. Resource management personnel attempt to obtain funds from customers when workcounts are suspended due to lack of funding. When these attempts are unsuccessful, resource management personnel write off the workcounts from ABS and no longer report the workcounts as suspended.

Analysis of Unfunded Workcounts

OJCS did not provide funding for services performed by the DFAS Indianapolis Network during FYs 2001 and 2002 because of a disagreement with WHS (Washington Headquarters Services) regarding who was responsible for providing the funds. As far back as 1993, funding for OJCS was provided to WHS to cover the cost of accounting services for OJCS. PBD 416 for FY 2001 included the estimated workload for OJCS in the WHS total estimate. According to personnel from the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer, funds were supplied to WHS according to the PBD 416 estimate and included amounts for DFAS Indianapolis Network services to OJCS.

Since at least 1995, WHS objected to the responsibility of paying for DFAS services provided to OJCS due to the burden the extra funds placed on their annual budget submitted to Congress. WHS cited DoD Regulation 7000.14-R, volume 11B, chapter 50, "Defense Working Capital Fund General Policies and Requirements," as support for their position. DoD Regulation 7000.14-R, volume 11B, chapter 50, states that each customer is responsible for reimbursing Defense Working Capital Fund activities for services performed for them. Beginning in FY 2001, after many unsuccessful discussions with OJCS and memorandums to the Under Secretary of Defense (Comptroller)/Chief Financial Officer, WHS discontinued making payments to resource management for services performed for OJCS. However, DFAS Indianapolis Network personnel continued to perform services throughout FYs 2001 and 2002 for OJCS without a funding document. OJCS did not pay for services received because OJCS contended that the funds for the services provided by the DFAS Indianapolis Network personnel were included in the funding the Under Secretary of Defense (Comptroller)/Chief Financial Officer provided to WHS.

DFAS wrote off \$661,000 in September 2002 for FY 2001 accounting services and \$551,000 in March 2003 for FY 2002 accounting services provided to OJCS. Table 2 shows the costs associated with the workload the DFAS Indianapolis Network personnel performed for OJCS during FYs 2001 and 2002. To ensure the most equitable method of recovering the lost revenue, WHS should pay the \$1.2 million for the unfunded workcounts performed by the DFAS Indianapolis Network.

Table 2. Costs Associated with Unfunded Workcounts Performed by the DFAS Indianapolis Network for OJCS During FYs 2001 and 2002

<u>Output</u>	<u>FY 2001</u>	<u>FY 2002</u>
Output 7-Travel Vouchers Paid	\$ 2,347	\$ 2,039
Output 8-Transportation Bills Paid	547	143
Output 9-Commercial Payments	82,981	98,360
Output 11-Direct Billable Hours for Accounting Services	558,219	439,575
Output 27-Travel Vouchers Paid – Defense Travel System	<u>17,369</u>	<u>10,599</u>
Total	\$661,463	\$550,716

DoD Regulation 7000.14-R, volume 11B, chapter 61, "Progress Billings, Reimbursements, and Revenue Recognition," stated that no work or service should be performed except on the basis of reimbursable orders received and accepted that constitute obligations of Federal Government ordering activities. The MIPR and subsequent acceptance by resource management personnel serve to obligate the funds of an entity. To avoid the consequences of a customer disagreement in the future, and to comply with the requirements set forth in DoD Regulation 7000.14-R, volume 11B, DFAS needs to establish and disseminate written policy addressing instances when customers do not pay for services provided. The policy should include the option to discontinue providing services to customers on a case-by-case basis, if needed. The failure of resource management personnel to collect the revenue for the suspended workcounts caused an increase in FY 2003 billing rates for all DFAS Indianapolis Network customers. DFAS should not provide services to customers who do not provide funding in a timely manner.

The effect of the resource management decision to write off workcounts valued at approximately \$1.2 million for FYs 2001 and 2002 for services provided to OJCS was to improperly augment, through provision of free services, the FYs 2001 and 2002 appropriations that were supposed to fund the expense for accounting services. The General Accounting Office has generally distinguished between the improper augmentation of an appropriation through the direct receipt of money as opposed to through the receipt of services, analyzing the former under the augmentation prohibition (31 U.S.C. 1301[a]) and the latter under the voluntary services prohibition (31 U.S.C. 1342). See Appendix B for further details regarding the requirements of section 1342. Since the issue involved gratuitous services rendered in an official capacity, and, therefore, could not have formed the basis for a future claim of payment upon Congress or the government, the decision to write-off the approximately \$1.2 million did not violate the voluntary services prohibition of the Anti-Deficiency Act (31 U.S.C. 1342).

Other Matters of Interest

During our audit, we identified seven additional customers who had suspended workcount balances from FY 2001. Over the course of FY 2001, the cost of services provided by the DFAS Indianapolis Network exceeded the funds available for transfer. However, by the end of FY 2002, all seven of the customers had provided MIPRs authorizing the transfer of additional funds. Subsequently, resource management personnel had removed the suspended workcount balances from ABS for the seven customers.

Management Comments on the Finding and Audit Response

WHS Comments. The Director, WHS indicated that the report incorrectly stated that PBDs 416 and 426 showed that WHS received funding to reimburse DFAS for services provided to OJCS during FYs 2001 and 2002. He stated that PBD 426 did not “provide” funding to WHS for the purpose of reimbursing DFAS on behalf of OJCS. The Director, WHS, also stated that WHS funding levels are set by PBD 071 and may be increased or decreased by other subject-specific decisions. He indicated that because DFAS Indianapolis Resource Management personnel billed OJCS directly, WHS did not establish reserves for payments to DFAS Indianapolis Resource Management on behalf of OJCS. The Director, WHS also stated that the report did not point out that OJCS has not followed long-established DoD budgetary policy for revolving funds, which requires that DFAS customers ensure that their budget submissions support all proposed DFAS purchases.

Under Secretary of Defense (Comptroller)/Chief Financial Officer Comments. Although not required to comment, the Director, Revolving Funds, Under Secretary of Defense (Comptroller)/Chief Financial Officer stated that OJCS did not pay the \$1.2 million for services rendered by DFAS because there was confusion about who should have paid for the services. The Director stated that it was past practice for the WHS to budget and pay for the services provided by DFAS to OJCS. The Director stated that she believes WHS had the funds in their budget to support OJCS, but that it is not clear from historical budget documents if either agency had funds in their budget to purchase the services. The Director, Revolving Funds concluded that it cannot be determined which organization should reimburse DFAS and that it is appropriate for DFAS to recoup the loss through its rates. She stated that further action is not needed because the loss has been recouped through increased FY 2002 and 2003 rates. In addition, the Director, Revolving Funds stated that starting in FY 2003, OJCS is identified as a separate customer by DFAS and funds the services provided by DFAS accordingly.

Audit Response. We agree that the report incorrectly stated that PBD 416 shows that WHS “received” funding to reimburse the DFAS Indianapolis Network. We have clarified the language in the finding to indicate that, according to personnel at the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer, funds were to be provided to DFAS Indianapolis Network customers based on the estimates in PBD 416. However, we do not agree that DFAS

Indianapolis Resource Management personnel billed OJCS directly. As previously stated, the ABS billing process is automatic, but ABS cannot generate the transfer of funds (i.e., generate the bill) until the customer provides a MIPR authorizing the transfer to resource management. ABS automatically suspends workcounts if funds are not available for transfer. A MIPR was not provided to DFAS Indianapolis for the accounting services rendered to OJCS during FYs 2001 and 2002. Therefore, DFAS could not generate a bill for the services so they suspended the workcounts. We agree that DFAS should be paid for the services provided to OJCS. We believe that PBD 416 clearly intended for WHS to receive the funding to pay DFAS for services provided to OJCS during FYs 2001 and 2002. However, neither the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer, WHS nor OJCS were able to provide funding documents to unequivocally show which agency actually received the funds to pay DFAS. Therefore, it is appropriate for DFAS to recoup the loss through changes in FYs 2002 and 2003 rates.

Recommendations, Management Comments, and Audit Response

Revised Recommendation. As a result of management comments, we revised draft Recommendation B.3. to clarify that the written policy should be a formalization of the currently informal process and that suspension of services for lack of payment should be an option, not an automatic action.

B.1. We recommend that the Director, Accounting Services, Army, Defense Finance and Accounting Service Indianapolis bill and collect the \$1.2 million from Washington Headquarters Services for services provided to the Office of the Joint Chiefs of Staff during FYs 2001 and 2002.

Management Comments. Although not required to comment, the Director, Revolving Funds, Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer provided comments stating that it is not clear if either WHS or OJCS received adequate funding to pay for the services DFAS provided to OJCS during FYs 2001 and 2002. The Director, Corporate Resources, DFAS nonconcurred and agreed with the position taken by the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer that it cannot be determined which organization should reimburse DFAS. She stated that the \$1.2 million loss has already been incorporated into the FY 2003 billing rates for DBHs. The Director, Corporate Resources also stated that DFAS, WHS, and OJCS have taken action to ensure payment for DBHs in the future.

Audit Response. While not the ideal solution, we agree with the Director, Revolving Funds, Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer that it cannot be determined which organization should reimburse DFAS. We also agree that it is appropriate for DFAS to recoup the loss through its rates. Further action is not needed because the loss is being recouped through increased FYs 2002 and 2003 rates.

B.2. We recommend that the Director, Washington Headquarters Services pay the Defense Finance and Accounting Service for services provided to the Office of the Joint Chiefs of Staff during FYs 2001 and 2002.

Management Comments. The Director, WHS nonconcurrent and stated that WHS should only be fiscally responsible for DFAS products and services actually received by WHS.

Audit Response. WHS comments are not responsive. However, we agree with the Director, Revolving Funds, Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer that it cannot be clearly determined which organization should reimburse DFAS and that it is appropriate for DFAS to recoup the loss through its rates. Further action is not needed because the loss was recouped through increased FYs 2002 and 2003 rates.

B.3. We recommend that the Director, Defense Finance and Accounting Service establish and disseminate a written policy addressing instances when customers do not pay for services provided. Include the option to discontinue providing services to customers on a case-by-case basis, if needed.

Management Comments. The Director, Corporate Resources, DFAS nonconcurrent and stated that DFAS management had discussed developing a policy in which service would be suspended pending receipt of funding. However, because the DFAS services fund the pay and logistical needs of the U.S. fighting forces, DFAS believes an interruption in service for non-payment is unacceptable because the potential negative impacts on U.S. fighting forces far exceed any benefits that could result from service interruption. She stated that failure to process or pay commercial transactions would only lead to interest penalties, and thus cause the customer's bill for services to increase.

The Director, Corporate Resources also stated that there is already a process in place to record and collect those monies. The process includes DFAS classifying workcounts performed for a customer in excess of funding as suspended workcounts. If, at the end of the fiscal year, a customer has suspended workcounts, DFAS works closely with the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer to seek final resolution with the customer.

Audit Response. The DFAS comments are partially responsive. Although we agree that a process is in place to record unpaid workcounts and collect the funds for those workcounts, the process is informal and, as evidenced by the failure to resolve issues related to uncompensated services provided to OJCS during FYs 2001 and 2002, the option to discontinue services to achieve a timely resolution is sometimes warranted. We do not advocate the suspension of services that would adversely impact the U.S. fighting forces. However, the suspension of accounting services may be appropriate under certain circumstances. Therefore, we revised the recommendation to clarify that the current informal process should be formalized in written policy.

The policy should at least include suspension of services as an option, not necessarily an automatic action, which can be applied on a case-by-case basis. We request that DFAS consider the revised recommendation and provide additional comments in response to the final report.

Appendix A. Scope and Methodology

The DFAS Indianapolis Network performed more than 3.8 million DBHs, valued at about \$253 million during FY 2001. The Defense Hotline complaint alleged that a high level DFAS official might have directed resource management personnel to reduce the Army's bill for accounting services received during FY 2001 by 122,000 DBHs.

We traced the processes from start to finish that resource management personnel used to record, collect, report, and bill DBHs. We identified all relevant procedures and systems used and their role in the DBH process through document examination and interviews with key resource management personnel. We also reviewed FY 2001 DBH workcount data from the various systems used in the processes.

We reviewed the statement provided by the complainant and met with the complainant to clarify issues relating to the allegation. We reviewed applicable laws, regulations, policies, and procedures relating to recording, collecting, reporting and billing for DBHs. We also obtained a detailed walkthrough of the processes by interviewing appropriate resource management personnel. Due to the lack of adequate documentation supporting and authorizing the adjustments made to DBHs, much of the information regarding the reasons for and approvals of the adjustments was obtained through interviews with resource management personnel involved in the DBH recording, collecting, reporting, and billing processes. We obtained and reviewed budgeting documents relating to DBHs. During the audit, we also noted that other customers were not promptly paying for DFAS services and we followed up on the reasons for this problem.

We performed this audit from March 2002 through March 2003 in accordance with generally accepted government auditing standards. We did not review the management control program because the audit was performed in response to an allegation made to the Defense Hotline and the scope was limited to the specific allegation. Therefore, review of the management control program was not an announced audit objective and we did not look at enough of the process to form conclusions about the management control program.

Use of Computer-Processed Data. We did not evaluate the general and application controls of the DFAS systems (DBH System, RADSS, the AWC System, and ABS) used to process direct billable hours data, although we relied on data produced by these systems to conduct the audit. Not evaluating controls did not affect the results of the audit. We performed alternative testing to establish data reliability by tracing sampled data from system to system through the processes for recording, collecting, reporting, and billing DBHs.

General Accounting Office High-Risk Area. The General Accounting Office has identified several high-risk areas in DoD. This report provides coverage of the DoD Financial Management high-risk area.

Prior Coverage

No prior coverage has been conducted on the subject during the last 5 years.

Appendix B. Allegation and Results

Allegation. In February 2002, the Office of the Assistant Inspector General for Auditing received an allegation from the Defense Hotline stating that a high level DFAS official might have directed resource management personnel to reduce the Army's bill for accounting services in FY 2001 by 122,000 DBHs. The allegation stated that the downward adjustment would have reduced the billable amount of accounting services provided to the Army by more than \$7 million. The complainant speculated that changes in the internal accounting systems for collecting and reporting workcounts apparently rendered previous estimates to the Army invalid. The complainant was also concerned about pressures from upper management to inappropriately lower customer costs as a method of maintaining good customer relations and about potential violations of the voluntary services provision of the Anti-Deficiency Act or other laws.

Audit Results. We substantiated that adjustments of 108,750 hours were made to the DFAS Indianapolis Network DBHs for FY 2001. We concluded that the substantiated adjustments were 13,250 hours less than the 122,000 hours contained in the allegation because resource management personnel were still in the process of making adjustments to the workcounts for DBHs when the allegation was submitted. There was a 108,750 hours difference between the direct productive hours totals in RADSS and the AWC system. The difference between the AWC system data and the RADSS data should only be work that DFAS Indianapolis Network personnel performed for DFAS. However, of the 108,750 hours, only 24,813 hours were appropriate adjustments for work DFAS Indianapolis Network personnel performed for DFAS. The remaining balance of 83,937 hours were inappropriate adjustments that primarily benefited the Army.

The impact of the resource management decision to make the 83,937 hours of inappropriate adjustments was to improperly augment, through provision of free services, the FYs 2001 and 2002 appropriations that were supposed to fund the expense for accounting services. The General Accounting Office has generally distinguished between the improper augmentation of an appropriation through the direct receipt of money as opposed to through the receipt of services, analyzing the former under the augmentation prohibition (31 U.S.C. 1301[a]) and the latter under the voluntary services prohibition (31 U.S.C. 1342). Section 1342 generally prohibits the acceptance of voluntary services or personal services exceeding that authorized by law. Case law draws a distinction between acceptance of "voluntary services" and "gratuitous services," indicating that the prohibition in section 1342 is not aimed at gratuitous services, but rather is intended to prevent the acceptance of unauthorized voluntary services that are likely to afford a basis for a future claim of payment upon Congress or the Government. Because the issue involved gratuitous services rendered in an official capacity, and, therefore, could not have formed the basis for a future claim of payment upon Congress or the Government, the decision to make 83,937 hours of inappropriate adjustments did not violate the voluntary services prohibition of the Anti-Deficiency Act (31 U.S.C. 1342). Also, the decision to write-off the FYs 2001 and 2002 suspended workcounts valued at \$1.2 million did not violate the voluntary services prohibition of the Anti-Deficiency Act (31 U.S.C. 1342). For additional details, see finding B.

Appendix C. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Comptroller)/Chief Financial Officer
Deputy Chief Financial Officer
Deputy Comptroller (Program/Budget)

Joint Staff

Director, Joint Staff

Department of the Army

Auditor General, Department of the Army

Department of the Navy

Auditor General, Department of the Navy

Department of the Air Force

Auditor General, Department of the Air Force

Other Defense Organizations

Director, Defense Finance and Accounting Service
Director, Washington Headquarters Services

Non-Defense Federal Organization

Office of Management and Budget

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

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 Reform
House Subcommittee on Government Efficiency and Financial Management, Committee on Government Reform
House Subcommittee on National Security, Emerging Threats, and International Relations, Committee on Government Reform
House Subcommittee on Technology, Information Policy, Intergovernmental Relations, and the Census, Committee on Government Reform

Defense Finance and Accounting Service Comments



DEFENSE FINANCE AND ACCOUNTING SERVICE
ARLINGTON

1931 JEFFERSON DAVIS HIGHWAY
ARLINGTON VA 22240-5291

JUL 18 2003



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

SUBJECT: Response to Draft Report Project Number D2002FI-0108, "Allegation of Improper
Accounting for Direct Billable Hours by DFAS," April 4, 2003

Our response to the subject draft report request is attached. The point of contact is
Mr. Alan Harms, (703) 607-0029 or DSN 327-0029.


Susan J. Grant
Director, Corporate Resources

Attachment:
As stated

Your Financial Partner @ Work
www.dfas.mil

Response to DODIG Audit Number D2002FI-0108:
Allegation of Improper Accounting for Direct Billable Hours by the Defense Finance and Accounting Service

Subject audit was an investigation into a complaint that the Defense Finance and Accounting Service's (DFAS') Indianapolis Center under-billed the Army for 120,000 hours of accounting services during Fiscal Year (FY) 2001.

The Inspector General's audit determined that the actual number of direct billable hours (DBHs) involved was 108,750, of which 83,113 were for services provided to the Army, 824 were for services provided to various Defense Agencies, and 24,813 were for accounting services DFAS provided to itself. The auditors also discovered, while investigating this allegation, that the Office of the Joint Chiefs of Staff (OJCS) and the Washington Headquarters Service (WHS) had not collectively reimbursed DFAS for all services provided to OJCS during FY01.

DFAS concurs with the auditors' findings that the Indianapolis Center did under-bill Army and Defense Agencies by the number of DBHs expressed above. There were mitigating factors that contributed to this event, including the division of the Indianapolis Center into two separate organizations, the deployment of a new, web-based DBH collection system, and the implementation of a new DBH customer allocation methodology. Those factors, however, do not warrant or justify not billing customers for all services performed.

DFAS, as a Working Capital Fund entity, obtains the revenue it requires for operation by seeking reimbursement from customers for actual services performed during the year said performance occurs. Those services, described in the form of workcounts, are billed on a monthly basis at pre-set rates. The non-recovery of costs incurred to perform those services has a negative affect on the Agency's net operating result (NOR), which impacts the billing rates for DFAS customers in future years. In this case, the impact of the Indianapolis Center not billing its customers in FY01 for the aforementioned DBHs is that DFAS sustained a loss of revenue of approximately \$5.6 million. This loss means that the FY03 billing rates would have to reflect a proportional adjustment for recovery to occur.

DFAS is developing and will implement an Agency-wide standing operating procedure (SOP) that will formalize the currently informal practice of collecting, allocating, and billing DBH workcounts to ensure non-billing of customer charges does not occur in the future. That SOP also will specify that appropriate audit trails are maintained to reflect the reasons and justifications for adjustments to customer billings when such adjustments become necessary.

Regarding the auditors' recommendation that DFAS bill and collect from the Army its \$5.5 million share of these unbilled charges, DFAS concurs. Based on guidance from OUSD (C) DFAS will adjust the FY 2005 DBH Billing Rates to recoup that portion of the \$5.5M which was not allocated to the Army in FY 2003. In addition, DFAS will reduce the FY 2005 DBH Billing Rates of those Agencies impacted by the \$5.5M loss.

DFAS concurs with the auditors' recommendation that no action be taken to recover the loss resulting from the non-billing of 824 direct billable hours to various Defense Agency customers. As indicated in the report, the dollar value of this loss, in proportion, is minimal and does not warrant the effort required to identify the customers involved and then to initiate collection procedures.

DFAS also agrees with the report's finding that DBHs for accounting services DFAS provides to itself should not be charged to external customers. These are operational costs and are normal parts doing business.

Regarding the non-payment by OJCS and WHS for services provided to the Office of the Joint Chiefs of Staff during FY01 and FY02, OUSD has addressed this matter in separate MEMORANDUM. That memorandum basically states it was not clear if either of the agencies in question received adequate funding for the services provided. In addition, those losses have already been incorporated into the DFAS FY03 Billing Rates for recovery. Finally, action has been taken by DFAS as well as the agencies in question in order to prevent this from occurring again in the future.

DFAS has discussed developing a policy in which service would be suspended pending receipt of funding, but the following reasons suggest that we not implement such a policy. Our services fund the pay and logistical needs of our fighting forces. A service interruption for non-payment would be unacceptable. The potential negative impacts on our fighting forces far exceed any positive that could result from this action. Second, failure to process or pay Commercial transactions would only lead to interest penalties, and thus cause the customers bill for service to grow. Finally, the amount of funding in question accounts for less than 1% of DFAS's total Revenue, and there is a process already in place to record and collect those monies. DFAS currently classifies work output performed for a customer in excess of funding as Suspended Workcounts. If at the end of the fiscal year a customer has Suspended Workcounts, DFAS works closely with OUSD (C) in order to seek final resolution with the customer involved.

DFAS appreciates the competent and thorough review conducted by the DOD Inspector General. Audits such as this help DFAS recognize and correct weaknesses in its processes and procedures, and, by making such corrections, will assist this Agency in becoming a World Class Provider of finance and accounting services.

Washington Headquarters Services Comments

Final Report
Reference



DEPARTMENT OF DEFENSE
WASHINGTON HEADQUARTERS SERVICES
1155 DEFENSE PENTAGON
WASHINGTON, DC 20301-1155

MAY 22 2003



MEMORANDUM FOR THE DIRECTOR, DEFENSE FINANCIAL AUDITING SERVICE,
DODIG

SUBJECT: Report on Unfunded Work Counts, Project No. D2002FI-0108

We non-concur with your recommendation that the Washington Headquarters Services (WHS) reimburse the Defense Finance and Accounting Service (DFAS) for accounting products and services provided to the Office of the Joint Chiefs of Staff (OJCS) during FY 2001 and FY 2002.

Your report incorrectly states that the WHS "received" funding to reimburse the OJCS for accounting products and services provided by the DFAS. PBD's 416 and 426 did not "provide" funding to the WHS for the purpose of reimbursing the DFAS on behalf of the OJCS. On the contrary, those decisions merely reflect estimates of services expected to be provided by customer, and the resources necessary to pay for services received. The WHS funding levels are set by PBD 071 and may be increased or decreased by other subject specific decisions.

Your report correctly asserts that each DFAS customer, who receives services, is required to reimburse the DFAS for all expenses incurred. The customer listing and workload count estimates in the decisions may not be completely accurate; however, this is irrelevant in terms of paying for services provided. The Financial Management Regulation (FMR) clearly states that working capital fund customers, such as the OJCS, are required to pay for products and services provided by working capital funds financed by DoD components, such as the DFAS. The WHS should only be fiscally accountable for the DFAS products and services WHS actually receives.

Of note, DFAS did not bill WHS for products and services rendered to the OJCS in FY 2001 and FY 2002. The DFAS prepared and issued bills directly to the OJCS for those years. For this reason, WHS did not establish reserves for payment to DFAS on behalf of the OJCS.

Additionally, your report fails to point out that the OJCS has not adhered to the long-established DoD budgetary policy for revolving funds. On an annual basis, the Under Secretary of Defense (Comptroller) issues, to all DoD components, a budget call memorandum, which supplements the budget estimates preparation provisions of the FMR. It clearly requires that DFAS customers ensure that their submissions support all proposed DFAS purchases.

We encourage you to consider that the OJCS be held liable for the accounting products and services they ordered and received from the DFAS during FY 2001 and FY 2002.

The opportunity to comment on this matter is appreciated.

Raymond F. DuBois
Director



Revised
Pages 11 and
12

Department of the Army Comments



DEPARTMENT OF THE ARMY
OFFICE OF THE ASSISTANT SECRETARY OF THE ARMY
FINANCIAL MANAGEMENT AND COMPTROLLER
108 ARMY PENTAGON
WASHINGTON DC 20310-0109



2 June 2003

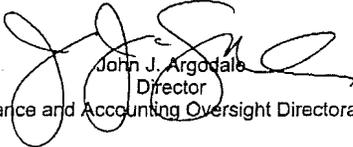
MEMORANDUM FOR DIRECTOR, DEFENSE FINANCIAL AUDITING SERVICE
DIRECTORATE, OFFICE OF THE INSPECTOR GENERAL, 400 ARMY NAVY DRIVE,
ARLINGTON, VIRGINIA 22202-4704

SUBJECT: Report on Allegation of Improper Accounting for Direct Billable
Hours by the Defense Finance and Accounting Service (Project No.
D2002FI-0108)

Reference your memorandum dated April 4, 2003 (enclosed).

We non-concur with recommendation A. a. The \$5.5 million is being recouped through
the FY2003 billing rates.

Point of contact on my staff is Mr. Wallace Riggins at DSN 223-3467 or commercial 703-
693-3467.


John J. Argodale
Director
Finance and Accounting Oversight Directorate

End

Under Secretary of Defense (Comptroller)/Chief Financial Officer Comments



COMPTROLLER
(Program/Budget)

OFFICE OF THE UNDER SECRETARY OF DEFENSE
1100 DEFENSE PENTAGON
WASHINGTON, DC 20301-1100

JUL 1 2003

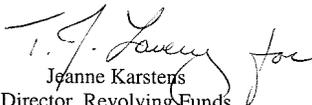
MEMORANDUM FOR DEPARTMENT OF DEFENSE INSPECTOR GENERAL,
(DIRECTOR, DEFENSE FINANCE AUDITING SERVICE)

SUBJECT: Allegation of Improper Accounting for Direct Billable Hours by the DFAS

Your office has recently concluded that Defense Finance and Accounting Service (DFAS) personnel performed work for the Office of the Joint Chief of Staff (OJCS) and did not receive payment of \$1,212.2 thousand for work performed. The value of work performed in FY 2001 is \$661.5 thousand, and the value for work performed in FY 2002 is \$550.7 thousand. The DFAS posted this amount as a loss and recouped it by increasing rates in FY 2002 and FY 2003.

The reason the OJCS did not pay for these services is because there was confusion on who should have paid these bills. It was past practice for the Washington Headquarters Service (WHS) to budget and pay for DFAS services that was rendered to OJCS. I believe WHS had funds in their budget to support OJCS, but it is not clear from historical budget documents if either Agency had dollars in their budget to purchase these services. Therefore, it can not be determined which organization should reimburse DFAS, and it is appropriate for DFAS to recoup this loss through all of their rates. No further action needs to be taken because these losses have already been recouped through increased rates. In addition, starting in FY 2003, the OJCS is identified as a separate customer by DFAS and funds DFAS services accordingly.

If you or your staff have any questions or need additional information regarding this issue, please contact Mr. Tom Kerr at (703) 697-1422.


Jeanne Karstens
Director, Revolving Funds

Team Members

The Defense Financial Auditing Service, Office of the Deputy Inspector General for Auditing of the Department of Defense prepared this report. Personnel of the Office of the Inspector General of the Department of Defense who contributed to the report are listed below.

Paul J. Granetto
Richard B. Bird
M. Leon Peek
Carmelo G. Ventimiglia
Cheri D. Givan
Ryan N. Pike
Sarah A. Buelo