

Inspector General

United States
Department of Defense



Hotline Review

March 22, 2011

Hotline Allegation Regarding the Failure
of Defense Contract Management Agency
Philadelphia to Settle an Audit of
a Significant Cost Accounting Change

Report No. D-2011-6-006

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Acronyms

DCAA	Defense Contract Audit Agency
DCMA	Defense Contract Management Agency
FAR	Federal Acquisition Regulation



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

MAR 22 2011

MEMORANDUM FOR DIRECTOR, DEFENSE CONTRACT MANAGEMENT AGENCY

SUBJECT: Hotline Allegation Regarding the Failure of Defense Contract Management Agency Philadelphia to Settle an Audit of a Significant Cost Accounting Change (Report No. D-2011-6-006)

We are providing this report for your information and use. We reviewed a DOD Hotline complaint and substantiated the allegation that a Defense Contract Management Agency (DCMA) contracting officer failed to take appropriate action on a 2002 Defense Contract Audit Agency (DCAA) report. We determined that the contracting officer failed to take any substantial action to either reach a settlement with the contractor or make a unilateral determination. Consequently, the contracting officer jeopardized the Government's ability to recoup \$7.4 million. In August 2010, we issued a Notice of Concern to the Director, DCMA, recommending that the agency take several immediate actions in response to our findings. As a result, DCMA took several actions including undertaking an agency-wide initiative to identify and take corrective action on other instances where contracting officers have not taken timely and appropriate action in response to DCAA audit reports.

In preparing this report, we considered management comments and actions in response to the August 2010 Notice of Concern that we issued to the Director, Defense Contract Management Agency. The management comments conformed to the requirements of DoD Directive 7650.3; therefore, additional comments are not required and we are issuing this report in final form.

We appreciate the courtesies extended to our staff. Questions should be directed to Ms. Carolyn R. Davis at (703) 604-8877 (DSN 664-8877), Carolyn.davis@dodig.mil.

A handwritten signature in blue ink, appearing to read "Randolph R. Stone", is positioned above the typed name.

Randolph R. Stone, SES
Deputy Inspector General
Policy and Oversight



Results in Brief: Failure of Defense Contract Management Agency Philadelphia to Settle an Audit of a Significant Cost Accounting Change

What We Did

We reviewed a DOD Hotline complaint alleging that a contracting officer at Defense Contract Management Agency (DCMA), Philadelphia, was negligent in addressing a Defense Contract Audit Agency (DCAA) report which stated that a DOD contractor owed the Government approximately \$7.4 million.

What We Found

We substantiated the allegation that a DCMA contracting officer failed to take appropriate action on a 2002 DCAA report, which stated that a DOD contractor owed the Government approximately \$7.4 million as a result of a cost accounting change. Our review disclosed that since September 2003, the contracting officer failed to take any substantial action to either reach a settlement with the contractor or make a unilateral determination and recover the amount due to the Government as a result of the cost accounting change. The contracting officer's failure to take timely action jeopardized the Government's ability to recoup those costs. The contracting officer did not comply with DOD Instruction 7640.02 when she dispositioned the DCAA audit report in the contract audit follow-up system and had not taken final action on that report. In August 2010, we issued a Notice of Concern to the Director, DCMA recommending that the agency take several immediate actions in response to our findings.

Management Actions

Following the issuance of our Notice of Concern, DCMA took several actions in response to our findings. The contracting officer reinstated the audit report in the contract audit follow-up system. On October 25, 2010, the contracting officer issued a final decision on the cost accounting change and took action to recover \$6.4 million owed to the Government. DCMA reduced the DCAA reported amount due of \$7.4 million to \$6.4 million, and we took no exception to the reduced amount. The Commander, DCMA Philadelphia, evaluated all audit reports assigned to this contracting officer and found that no others were languishing without cause. To enhance management oversight and controls, DCMA Philadelphia added a mechanism to monitor underlying audit issues and track disclosure statement audits. DCMA Philadelphia also reassessed the contracting officer's appointment authority and elected to retain that authority. Finally, DCMA undertook an agency-wide initiative to identify and take corrective action on other instances where contracting officers have not taken timely and appropriate action in response to DCAA audit reports.

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Introduction

Objective

We conducted this review to determine whether we could substantiate a DOD Hotline complaint concerning a Defense Contract Management Agency (DCMA) contracting officer stationed in Philadelphia, Pennsylvania. The complainant alleged that the contracting officer failed to take action on a 2002 Defense Contract Audit Agency (DCAA) audit report, which reported that a DOD contractor owed the Government approximately \$7.4 million as a result of the contractor's cost accounting change.

See Appendix A for details regarding our scope and methodology.

Background

Defense Contract Audit Agency (DCAA)

DCAA performs all necessary contract audits for DOD and provides accounting and financial advisory services to DOD Components regarding DOD contracts and subcontracts. DCAA issues reports resulting from several types of audits, such as audits of contractor compliance with cost accounting standards established by the Cost Accounting Standards Board. DCAA performs these audits to ensure that contractors adequately describe the practice they use to estimate, accumulate and record contract costs, and that these practices comply with the cost accounting standards. When a contractor proposes to change a cost accounting practice, DCAA will audit the change to determine if it results in increased costs paid by the Government.

Defense Contract Management Agency (DCMA)

DCMA works directly with Defense suppliers to help ensure that DOD, Federal, and allied government supplies and services are delivered on time, at the projected cost, and meet all performance requirements. DCMA serves as the in-plant representative for DOD-buying agencies, both during the initial stages of the acquisition cycle and throughout the life of the resulting contracts, and administers more than 300,000 active government contracts. DCMA contracting officer responsibilities include completing the resolution and the disposition of contract audit reports issued by DCAA on behalf of the Army, Navy, Air Force, Defense Logistics Agency, and other DOD agencies. The allegation addressed in this report involves a DCMA office located in Philadelphia, Pennsylvania (referred to as "DCMA Philadelphia" in this report).

Department of Defense Instruction 7640.02

DOD Instruction 7640.02, "Policy for Follow-up on Contract Audit Reports," August 22, 2008, prescribes the responsibilities, reporting requirements, and follow-up procedures on audit reports that DCAA issues. The Instruction (as well as predecessor DOD Directive No. 7640.2, February 12, 1988) requires contracting officers to complete the resolution and disposition of DCAA audit reports in a timely manner. Generally, contracting officers should complete the

resolution and disposition of DCAA audit reports within 6 months and 12 months, respectively. In dispositioning a DCAA audit report, contracting officers must prepare a post-negotiation memorandum covering the actions they took in response to significant audit report findings, including the underlying rationale for such actions.

The Instruction also requires that DOD Components, including DCMA, maintain up-to-date records on the status of actions taken in response to certain types of audit reports defined as “reportable,” and semiannually furnish the status of those actions to the DOD Inspector General. DOD Components utilize an electronic system referred to as the “contract audit follow-up system” for this purpose. Once a contracting officer completes all necessary actions on an audit report, the contracting officer changes the audit status to “dispositioned” in the contract audit follow-up system and the audit is subsequently dropped from future reporting to the DOD Inspector General.

Finding

Untimely Action in Settling a Contract Audit Report

We substantiated the allegation that a DCMA contracting officer stationed in Philadelphia, Pennsylvania, failed to take timely action on a 2002 DCAA audit report in which DCAA reported that a DOD contractor owed the Government approximately \$7.4 million as a result of a cost accounting change.

Background

On June 14, 2002, DCAA reported that a cost accounting change implemented by a DOD contractor resulted in \$7.4 million in increased costs to the Government. In a September 17, 2003 letter to the contractor, the contracting officer ruled that the accounting change was not desirable to the Government, and as a result, the contractor must pay for any increased costs resulting from the change in accordance with Federal Acquisition Regulation (FAR) 30.603-2. The contracting officer proposed an amount due to the Government of \$6.9 million, \$500,000 less than the \$7.4 million originally reported by DCAA based on additional information that the contractor provided. DCAA agreed with the revised amount.

The September 17, 2003 letter also stated that if the parties could not reach an agreement on the appropriate amount due to the Government within a reasonable time, the contracting officer was "...prepared to make a unilateral determination subject to appeal as provided for in the Disputes clause, FAR 52.233." However, as of September 2010 (7 years later), the contracting officer had yet to reach an agreement or issue a unilateral decision.

Our Review

We researched applicable regulations, DOD Instructions, and agency policies. In addition, we interviewed the contracting officer and several other DCMA and DCAA officials. We also obtained and reviewed DCMA files associated with this cost accounting change.

FAR Subpart 30.6, *CAS Administration*, addresses contracting officer responsibilities regarding the administration of Cost Accounting Standard issues. FAR 30.604 outlines steps that contracting officers must take to process cost accounting changes, and FAR 30.606 identifies actions that contracting officers must take to resolve the amount due to the Government for cost accounting changes. When a contracting officer and a contractor cannot reach agreement on the cost impact of a cost accounting change, FAR 30.606(c)(6) requires the contracting officer to issue a final decision in accordance with FAR 33.211 and to unilaterally adjust affected contracts.

Our review of the DCMA file disclosed that in the 7 years since the contracting officer's September 17, 2003 letter to the contractor, the contracting officer had not taken any substantial action to resolve the cost accounting change and recoup the amount due to the Government in accordance with FAR 30.606. The contracting officer stated that she met with the contractor

several times over the 7-year period in an attempt to resolve various issues underlying the cost accounting change, but that the parties could not reach an agreement. The Contracts Director at DCMA Philadelphia stated that the contracting officer's workload required her to prioritize many tasks, and that the officer's priorities were consistent with agency and customer priorities.

We reject the premise that the contracting officer justifiably placed the cost accounting change, worth up to \$7.4 million, in low priority status over a 7-year period. Failure of the contracting officer to take timely and effective action in resolving the cost accounting change is inexcusable, and the extent of the delay could have jeopardized the ability of the Government to recoup the amount owed. For example, FAR limits the time that the Government can initiate a claim against a DOD contractor. Also, resolution of audit report issues become more difficult over time as individuals with a detailed understanding of the issues may transfer or retire, or the records may become lost.

In neglecting to take timely action on the DCAA audit report, the contracting officer also failed to comply with DOD Instruction 7640.02, Enclosure 3, paragraph 3(a) [and predecessor DOD Directive 7640.2 dated February 12, 1988], which requires that contracting officers disposition audit reports within 12 months. In addition, the contracting officer did not comply with DOD Instruction 7640.02 when she changed the status of the audit report to "dispositioned" in the contract audit follow-up system on March 30, 2009. DOD Instruction 7640.02, Glossary, states that a disposition occurs when the contracting officer determines final action on a cost impact proposal. As of March 30, 2009, the contracting officer had not determined the final action. During our review, DCMA acknowledged that dispositioning the audit report was incorrect and the contracting officer reinstated the audit report in the contract audit follow-up system.

Prior Reporting of Similar DCMA Philadelphia Deficiencies

On April 8, 2009, under Report No. D-2009-6-004, we reported that DCMA Philadelphia contracting officers did not process Cost Accounting Standard noncompliance audit reports in accordance with FAR 30.605, Processing Noncompliances. We found that failure of contracting officers to take timely and effective action in response to Cost Accounting Standard noncompliance reports caused significant delays in correcting potentially noncompliant practices and recovering any increased costs due to the Government. Finally, we noted several instances where DCMA Philadelphia contracting officers did not take timely action on several other audit reports, and that DCMA lacked adequate management controls for timely resolving audit reports in accordance with DOD Instruction 7640.02.

Repeated failure of DCMA to take timely action on DCAA audit reports demonstrates the need for DCMA management to take immediate and substantive corrective actions.

Notice of Concern, Management Actions, and Our Response.

On August 17, 2010, we issued a “Notice of Concern”¹ to the Director, DCMA covering the lack of timeliness on the part of the contracting officer to settle the audit findings and recoup the amount due to the Government reported by DCAA. We recommended several corrective actions (see Appendix B). In an August 30, 2010 memorandum, the Director, DCMA, provided a comprehensive response to our Notice of Concern which included specific action plans for recouping the amount due to the Government and improving the agency’s controls to help prevent reoccurrences (see Appendix C). Since the August 30, 2010 memorandum, DCMA aggressively implemented several corrective actions. Discussed below is a summary of management actions DCMA took based on our recommendations and our related responses to those management actions.

1. **Recommendation:** Oversee and ensure the actions needed to settle and recoup the amount due to the Government for the contractor’s cost accounting change.

Management Actions

On October 25, 2010, the contracting officer issued a final (unilateral) decision in accordance with FAR Part 33 and the Contract Disputes Act of 1978, stating in part that the contractor owed the Government \$6.4 million as a result of the cost accounting change. The contracting officer reduced the amount due from \$6.9 million to \$6.4 million based on the elimination of interest due. Based on advice from DCMA Headquarters, the contracting officer determined that the Government could not charge the contractor for accumulated interest in this case. In February 2011, the contracting officer transferred the amount due to the Defense Finance and Accounting Service for collection.

Our Response

The management actions satisfy the recommendation. No additional comments are required. We take no exception to the revised amount due to the Government of \$6.4 million.

2. **Recommendation:** Determine that no other DCAA audit reports assigned to the contracting officer for action are languishing without cause.

Management Actions

DCMA performed a review of the contracting officer’s workload and determined that no other audit reports assigned to the contracting officer were languishing without cause.

¹ A Notice of Concern is issued to alert DOD management of significant findings that require immediate attention. By issuing a Notice of Concern, DOD management officials can take proactive steps to mitigate the reported issue.

In addition, with assistance from DCAA, DCMA undertook a “Cost Recovery Initiative,” to identify all unresolved audit issues agency-wide and is actively track the resolution of each audit issue. This initiative is in progress.

Our Response

The Director, DCMA’s comments are responsive. No additional comments are required. Under a separate review (Project No. D2011-DIPOAI-0188.000), we will evaluate the appropriateness of efforts used to implement the “Cost Recovery Initiative,” and determine whether DCMA established effective controls agency-wide to ensure that contract audit reports are resolved and dispositioned in a timely manner.

We did not reevaluate the individual contracting officer's workload to verify that the officer had no other languishing audits. Instead, we will focus on DCMA’s efforts to correct this issue on an agency-wide basis under the Cost Recovery Initiative.

3. **Recommendation:** Evaluate and reassess the appointment authority previously granted to the contracting officer under Federal Acquisition Regulation 1.603, Selection, Appointment and Termination of Appointment.

Management Actions

The Director, DCMA reassessed the appointment authority of the contracting officer and decided not to terminate the authority.

Our Response

The Director, DCMA’s comments are responsive. No additional comments are required. For the record, we asked DCMA to provide the basis for its decision and to let us know whether DCMA considered other appropriate administrative action.

4. **Recommendation:** Evaluate and reassess the managerial oversight practiced by the DCMA Philadelphia office which enabled a significant amount due to the Government to languish over 8 years.

Management Actions

DCMA evaluated the management oversight at Boeing Philadelphia and found that the agency lacked a mechanism for tracking underlying audit issues. Accordingly, DCMA worked in concert with DCAA to develop an agency-wide mechanism for effectively tracking timely resolution. DCMA has since added this mechanism.

Our Response

The Director, DCMA’s comments are responsive. No additional comments are required. We will review the effectiveness of the mechanism as part of our review of the Cost Recovery Initiative.

-
5. **Recommendation:** Reestablish a system of management controls at the DCMA Philadelphia office to identify, investigate, and resolve DCAA audit reports in accordance with the FAR and DOD Instruction 7640.02.

Management Actions

DCMA believes that it has an appropriate system of management controls. However, based on its reassessment, DCMA found that it needed to track disclosure statement audits (5-digit audit code 19100) even though they are not reportable under DOD Instruction 7640.02. Accordingly, DCMA asked DCAA to include disclosure statement audits within the contract audit follow-up system, and DCMA has begun tracking these audits.

Our Response

The Director, DCMA's comments are responsive. No additional comments are required. We will review the effectiveness of management controls agency-wide as part of our review of the Cost Recovery Initiative.

Other Matters

The August 30, 2010 DCMA letter (Appendix C) recommends that the Office of the Inspector General revise DOD Instruction 7640.02, *Policy for Follow-up on Contract Audit Reports*, to:

- provide new criteria for the disposition of contract audit reports issued on Cost Accounting Standard disclosure statements and Cost Accounting Standard noncompliance audits; and
- require the tracking of contract audit reports concerning audits of contractor disclosure statements.

On March 3, 2011, we initiated Project No. D2011-DIP0AI-0113.000 to review, and where necessary, revise DOD Instruction 7640.02. We will consider DCMA's recommendations as part of the work performed under this project.

Appendix A. Scope and Methodology

We reviewed the DOD Hotline complaint to determine if we could substantiate the allegations. As part of our review, we:

- obtained and reviewed data included in the contract audit follow-up system for the DCMA Philadelphia office;
- obtained and reviewed DCMA contract file documentation;
- interviewed contracting officials, including the contracting officer addressed in the complaint, other DCMA Philadelphia officials, and DCAA officials involved in the issue;
- coordinated with the DOD Hotline complainant; and
- reviewed applicable laws, regulations, DOD Instructions, and DCMA policies and procedures.

We performed this review from April 2010 through February 2011.

Use of Computer-Processed Data

We did not rely on computer-processed data as part of our review.

Prior Coverage

In the last 5 years, we have issued five other reports on DCMA contracting officer actions in response to DCAA audit reports.

- Department of Defense Inspector General Report No. D-2010-6-002, “Report on Allegation of Unsatisfactory Conditions Regarding Actions by the Defense Contract Management Agency, Earned Value Management Center,” July 28, 2010.
- Department of Defense Inspector General Report No. D-2009-6-008, “Report on Hotline Complaint Regarding the Actions by a Contracting Officer at the Defense Contract Management Agency, East Hartford Office,” August 31, 2009.
- Department of Defense Inspector General Report No. D-2009-6-004, Defense Contract Management Agency Actions on Audits of Cost Accounting Standards and Internal Control Systems at DOD Contractors Involved in Iraq Reconstruction Activities,” April 8, 2009.

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- Department of Defense Inspector General Report No. D-2007-6-010, “Report of Hotline Allegation Regarding the Reimbursement of Settlement Costs at Defense Contract Management Agency Melbourne,” September 28, 2007.
 - Department of Defense Inspector General Report No. D-2007-6-009, “Actions on Reportable Contract Audit Reports by the Defense Contract Management Agency's Northrop Grumman El Segundo Office,” September 28, 2007.

Appendix B. DOD Inspector General Notice of Concern



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

AUG 17 2010

MEMORANDUM FOR DIRECTOR, DEFENSE CONTRACT MANAGEMENT
AGENCY

SUBJECT: Notice of Concern – Timeliness in Addressing Contract Audit Follow Up
on a DCAA Report to DCMA Boeing Philadelphia

Our review of a Department of Defense Hotline complaint has identified a reportable Defense Contract Audit Agency contract audit report that has languished with Defense Contract Management Agency divisional administrative contracting officers since 2002. Timely resolution of contract audit reports is critical to protect the Department and the taxpayer, particularly a report that could have resulted in significant net savings to the United States Government. Delays relating to investigations, litigation, and requests to delay administrative actions until such activities are settled are understandable. Reports languishing due to 'other priority workload' and unwarranted contractor delays demand corrective action.

In Audit Report No. 6341-2002D19500001, dated June 14, 2002, the auditor reported a cost impact of \$7.4 million resulting from a January 1, 2001 unilateral cost accounting change implemented by a Boeing Company business segment. Based in part on the DCAA findings, the divisional administrative contracting officer issued on September 17, 2003 a determination letter to the contractor identifying \$6.9 million in aggregate increased cost. The divisional administrative contracting officer deemed the changes adequate and compliant, but not desirable to the Government. Under such a determination, the United States Government does not pay increased costs. The September 17, 2003 letter also stated that if the parties could not reach agreement on an appropriate cost adjustment within a reasonable time, the divisional administrative contracting officer was "...prepared to issue a unilateral determination subject to appeal as provided for in the Disputes clause, FAR 52.233."

We found that in the eight years since the contract audit report was issued; the divisional administrative contracting officer has neither (i) reached a settlement with Boeing nor (ii) made a unilateral determination in accordance with FAR 52.233-1, hence failing to recoup the \$7.4 million in increased cost.

DoD Instruction 7640.02 states contracting officers shall reach settlement within one year of receiving an audit report with findings. Where mutual agreement between

the contractor and government contracting officers is not achieved, contracting officials must provide the contractor a final decision. Regarding claims filed to contractors in the form of a final decision, the Contract Disputes Act states, "Each claim by the government against a contractor relating to a contract shall be submitted within 6 years after the accrual of a claim." Delays in resolving potential disputes can leave contracting officers holding unasserted claims beyond the 6 year statute of limitations. Exceeding the 6 year period can jeopardize the contracting officer's ability to recover increased costs on United States Government contracts.

With regard to the languishing audit report identified at the Boeing Philadelphia contract management office, we recommend DCMA management:

1. Oversee and ensure the actions taken by the contract management office to settle and recover the approximately \$7.4 million outstanding cost impact identified in DCAA Report No. 6341-2002D19500001 comply with FAR 30.6 *CAS Administration* and, where necessary, FAR 33.2 *Disputes and Appeals*.
2. Take appropriate corrective actions to:
 - a. Determine that no other contract audit reports received by the divisional administrative contracting officer since 2002 are languishing without cause.
 - b. Evaluate and reassess the Appointment authority previously granted the divisional administrative contracting officer under FAR 1.603 *Selection, appointment and termination of appointment*.
 - c. Evaluate and reassess the managerial oversight practiced by the Boeing Philadelphia contract management office that enabled a potential savings of approximately \$7.4 million to the United States Government that has languished for over 8 years.
3. Re-establish a system of management controls at the Boeing Philadelphia contract management office to identify, investigate and resolve contract audit reports in accordance with the requirement of the Federal Acquisition Regulation and DoD Instruction 7640.02

We issue a Notice of Concern to alert DoD management of significant findings that we believe require immediate attention. The finding that generated this Notice of Concern and any corrective action taken by management will be included in an upcoming OIG draft report. By issuing a Notice of Concern, DoD management can take proactive steps to mitigate the reported issue.

Please provide a response to our recommendations by August 31, 2010. If you have any questions regarding this memorandum, please contact me at (703) 604-8877 or Ms. Meredith Long-Morin at (703) 604-8739 (meredith.morin@dodig.mil).

Carolyn R. Davis

Carolyn R. Davis
Assistant Inspector General
for Audit Policy and Oversight

Appendix C. Defense Contract Management Agency Response to Notice of Concern



DEFENSE CONTRACT MANAGEMENT AGENCY

6350 Walker Lane, Suite 300
Alexandria, Virginia 22310-3241

AUG 30 2010

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDIT POLICY AND OVERSIGHT

SUBJECT: Notice of Concern – Timeliness in Addressing Contract Audit Follow Up (CAFU) on DCAA Report to DCMA Boeing Philadelphia

This is in response to your August 17, 2010 Notice of Concern regarding the timeliness of actions taken by DCMA Boeing Philadelphia to recoup the \$7.4 million of increased costs for non-desirable accounting changes reported in DCAA Audit Report No. 6341-2002D19500001 dated June 14, 2002.

I fully agree that your findings represent a significant deficiency in our control procedures for resolving DCAA audit findings. DCMA must ensure that all audit findings and recommendations are resolved in a timely manner consistent with legal statutes, regulations, and Department of Defense (DoD) policy. DCMA has taken aggressive actions over the past two years to reduce the number of overage unresolved audits. This fiscal year we reduced the number of overage unresolved audits from 453 to 386 as of June 30, 2010. While we have made progress, the Agency continues to have an unacceptable number of overage audits. As a result, we reported overage audits as a material weakness in the Agency's 2010 Statement of Assurance and made a commitment to the Department that we will reduce the overage audits by the end of fiscal year 2011.

To improve performance, we are targeting the oldest audits first. In April 2010, I personally reviewed all of the overage audits reported in the CAFU system that were more than four years overage for "disposition." As you know, the Boeing Philadelphia Divisional Administrative Contracting Officer (DACO) had inappropriately closed the subject audit in CAFU. As a result, that audit was not included in my review. In September, we will review the overage audits more than three years overage for "disposition" and the "unresolved" audits that are one year past the audit report date. In addition we have tasked the workforce to provide us plans for reducing the overage audits more than two years overage for "disposition." A copy of that tasking memorandum is attached. The memorandum also alerts the workforce about the subsequent reviews we have scheduled for fiscal year 2011.

Last year, I established an Agency-wide CAFU quality assurance plan. The plan implemented mandatory standard CAFU performance objectives for our contracting workforce, key internal controls for managing CAFU and, annual assessments of actions taken and planned to resolve and disposition audit findings. The plan also provides for an assessment of our contracting officers' requisite specialized knowledge, experience, training, business acumen, and judgment to execute their duties. We will have the results of our first annual assessments by December 30, 2010.

Clearly, your audit findings highlight the need for more proactive oversight. Based on our assessment of your potential findings at DCMA Boeing Philadelphia, we initiated discussions with our Boeing Defense Services DACO in May. An additional 94 unresolved CAS accounting changes cost impacts were identified that were not tracked and not required to be tracked in the CAFU system. As such, we learned that we cannot rely on the CAFU system to track unresolved cost impacts as discussed below.

In accordance with the DoDI 7640.02, Policy for Follow-Up on Contract Audit Reports, Cost Accounting Standards (CAS) noncompliance audits (DCAA activity code 19200) are "dispositioned" in CAFU when the administrative contracting officer (ACO) issues a written final determination of compliance or noncompliance. Any associated CAS cost impact audit reports are "dispositioned" when the ACO executes a bilateral modification that resolves the cost impact or issues a final decision and unilaterally adjusts the contracts in accordance with FAR 30.606, Resolving Cost Impacts. In the period between disposition of the CAS noncompliance report and receipt of the audit report on the CAS cost impact, CAFU does not track the unresolved cost impacts. In addition, audits on contractors' CAS Disclosure Statements (DCAA activity code 19100) are not even tracked in CAFU. Like the CAS noncompliance audits, many of these audits subsequently result in required cost impacts.

Some of the newly identified 94 unresolved cost impacts date back to accounting changes made as early as 2000. For most, the contractor's initial cost impact proposals were inadequate and the ACOs have been attempting to get adequate cost impact proposals. We are working jointly with DCAA to expedite resolution of these cost impacts.

Based on this, I am taking immediate action to fully assess the severity of this situation. As shown in the attached tasking memorandum, we are implementing a

three phase strategy to fully assess the severity of, and reasons for, this situation. Phase one will identify the comprehensive list of unresolved cost impacts. Phase two will identify the unresolved cost impacts with statute of limitations issues and reasons contractual remedies were not pursued. Phase three will be to put in place a resolution plan based on the findings from phases one and two.

As we proceed, we will work with DCAA to ensure that we have adequate controls and procedures to prevent future occurrences. While the Department currently tracks the resolution of individual audits, the Department does not currently track the overall resolution of the underlying issue. As the six year statute of limitations applies to the resolution of the underlying issues, we are working with DCAA to develop a mechanism to effectively track timely resolution of the underlying issues.

While we can and will develop a tracking mechanism, the Department would be best served by a Department-level tracking mechanism as this situation is not unique to DCMA. In the short term, we recommend that you consider revising the DoDI 7640.02 to require tracking of the CAS Disclosure Statement audits (DCAA activity code 19100) and provide new criteria for the "disposition" of CAS noncompliance audits (DCAA 19200) and CAS Disclosure Statement audits. Specifically, we recommend that the "disposition" instructions for both be either an ACO's written determination that a cost impact is required or receipt of the audit report on the resulting cost impact. For long-term, we recommend that you consider adding a feature to CAFU to track resolution of the underlying audit issue.

With regard to the languishing audit report you identified at Boeing Philadelphia, I fully agree with your recommendations as discussed below.

OIG Recommendation 1: Oversee and ensure the actions taken by the contract management office to settle and recover the approximately \$7.4 million outstanding cost impact identified in DCAA Report No. 6341-2002D19500001 comply with FAR 30.6, CAS Administration and, where necessary FAR 33.2, Disputes and Appeals.

DCMA Response: Concur. The Director, Contracts Policy, and a HQ Associate General Counsel will conduct weekly status meetings with the CMO and the action will be subjected to an Executive Director, Contracts, board of review to ensure the resulting action complies with the referenced FAR requirements.

OIG Recommendation 2a: Take appropriate corrective actions to determine that no other contract audit reports received by the DACO since 2002 are languishing without cause.

DCMA Response: Concur. We will work jointly with DCAA to ensure that we identify all unresolved audits and underlying audit issues at DCMA Boeing Philadelphia, including those assigned to the DACO. In addition, we will actively monitor the resolution of the audits and audit issues.

OIG Recommendation 2b: Take appropriate corrective actions to evaluate and reassess the Appointment authority previously granted to the DACO under FAR 1.603, Selection, Appointment, and Termination of Appointment.

DCMA Response: Concur. The Contracts Director for the Operations Directorate will assess the DACO's appointment, consider whether any actions should be taken, and provide a recommendation to the Executive Director, Contracts for decision.

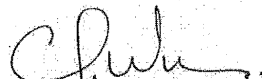
OIG Recommendation 2c: Take appropriate corrective actions to evaluate and reassess the management oversight practiced by the Boeing Philadelphia contract management office that enabled a potential savings of approximately \$7.4 million to the United States Government that has languished for over 8 years.

DCMA Response: Concur. We will evaluate and reassess the management oversight at Boeing Philadelphia. Our policy requires the DACO to get the CMO Contracts Director's approval of actions planned and taken to disposition audits in CAFU. As a part of our assessment, we will determine if the CMO complied with the policy and whether additional controls are needed to ensure that audits are appropriately dispositioned. However, as discussed above, we will also develop a mechanism for tracking the unresolved underlying audit issues to ensure appropriate visibility and timely resolution.

OIG Recommendation 3: Re-establish a system of management controls at the Boeing Philadelphia contract management office to identify, investigate and resolve contract audit reports in accordance with the requirements of the Federal Acquisition Regulation and DoD Instruction 7640.02.

DCMA Response: Concur. While we generally believe that our CAFU policy provides the appropriate management controls, we will reassess the policy and determine if additional controls and procedures are needed.

Finally, I think it is once again worth noting that although disappointing, the issues you have identified are often complex and time consuming to resolve. It is issues like this that underscore the importance of the actions we are taking to grow the workforce and ensure it is trained and capable. We continue diligently down this path to recovery. Please direct any comments or questions to Robin Schulze, Director, Contracts Policy, at (703) 428-1708 or robin.schulze@dema.mil.



Charlie E. Williams, Jr.
Director



Inspector General Department of Defense

