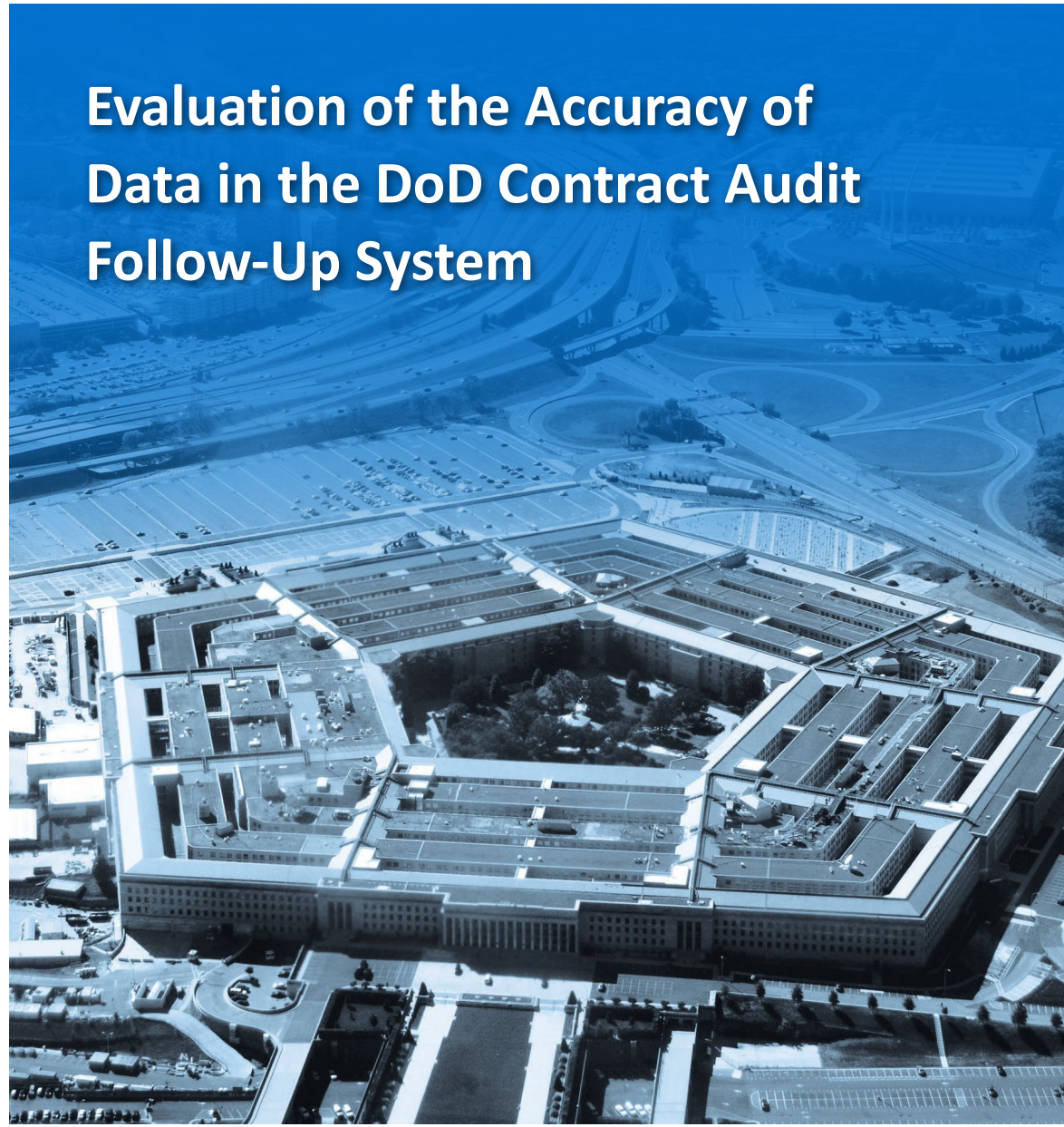




# INSPECTOR GENERAL

*U.S. Department of Defense*

MAY 13, 2016



## Evaluation of the Accuracy of Data in the DoD Contract Audit Follow-Up System

INTEGRITY ★ EFFICIENCY ★ ACCOUNTABILITY ★ EXCELLENCE

INTEGRITY ★ EFFICIENCY ★ ACCOUNTABILITY ★ EXCELLENCE

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# Results in Brief

## *Evaluation of the Accuracy of Data in the DoD Contract Audit Follow-Up System*

May 13, 2016

### Objective

We evaluated the accuracy of data in the Contract Audit Follow-Up (CAFU) System, which DoD Components use to track and manage the status of actions that contracting officers take in response to Defense Contract Audit Agency (DCAA) audit reports. During FY 2014, DCAA audit reports questioned \$10.7 billion in proposed DoD contractor costs. The data residing in CAFU are summarized and included in the DoD Inspector General Semiannual Report (SAR) to Congress. The data in CAFU need to be accurate to ensure that reported DCAA audit findings are timely and appropriately resolved and that the SAR is correct.

### Finding

Of the 50 CAFU reportable audit records we tested, 41 records (82 percent) included inaccurate information in one or more data fields. Each record includes up to 20 data fields with information on each DCAA report. In total, 100 data fields had errors. For example, we found 10 errors associated with the "Questioned Cost" data field because the amounts in the field did not comply with DoD Instruction 7640.02, "Policy for Follow-up on Contract Audit Reports," April 15, 2015, which establishes record-keeping and reporting requirements for reportable contract audits. The errors caused a \$2.6 million overstatement of Questioned Cost in CAFU.

### Finding (cont'd)

In addition, in 15 instances, DCMA contracting officers entered inaccurate Questioned Cost Sustained amounts in CAFU that resulted in overstating Questioned Cost Sustained in CAFU by \$8.4 million.

We have also detected errors in CAFU information while compiling CAFU information for the SAR. For example, a CAFU error could have caused a \$1.97 billion overstatement of Questioned Cost Sustained in the March 31, 2014, SAR if we had not detected it.

CAFU data errors adversely impact DoD management's ability to rely on CAFU as a tool for tracking contracting officer actions on DCAA audit reports. The frequency of the CAFU errors demonstrates the need for DCAA and DCMA to improve CAFU-related procedures and internal controls.

### Recommendations

We recommend that the Directors of DCAA and DCMA provide refresher training and modify agency procedures and related internal controls to improve CAFU data accuracy and help ensure compliance with DoD Instruction 7640.02. For example, we recommend that DCMA modify its procedures to ensure contracting officers complete required actions on all DCAA findings before contracting officers close an audit record in the CAFU system (see Recommendation 3.b).

### Management Comments and Our Response

The Directors of DCMA and DCAA fully agreed with the recommendations, except the Director, DCMA agreed in part to Recommendation 3.b. DCMA's plan to update DCMA Instruction 126 in response to Recommendation 3.b would allow contracting officers to inappropriately close a CAFU record before all questioned costs have been addressed. The update would not comply with DoD Instruction 7640.02 and be contrary to DoD's interest in ensuring that contracting officers appropriately address all audit findings. Therefore, we request that the Director, DCMA provide additional comments on Recommendation 3.b. Please see the Recommendations Table.

## ***Recommendations Table***

<b>Management</b>	<b>Recommendations Requiring Comment</b>	<b>No Additional Comments Required</b>
Director, Defense Contract Audit Agency		1, 2.a, 2.b, 2.c, and 2.d
Director, Defense Contract Management Agency	3.b	1, 3.a

Please provide Management Comments by June 13, 2016.



**INSPECTOR GENERAL  
DEPARTMENT OF DEFENSE  
4800 MARK CENTER DRIVE  
ALEXANDRIA, VIRGINIA 22350-1500**

May 13, 2016

MEMORANDUM FOR DIRECTOR, DEFENSE CONTRACT AUDIT AGENCY  
DIRECTOR, DEFENSE CONTRACT MANAGEMENT AGENCY

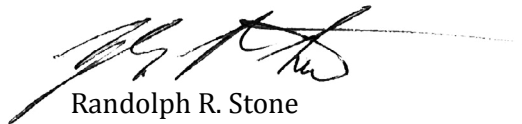
SUBJECT: Evaluation of the Accuracy of Data in the DoD Contract Audit Follow-Up System  
(Report No. DODIG-2016-091)

We are providing this report for your review and comment. We evaluated the accuracy of data residing in the DoD Contract Audit Follow-Up (CAFU) System, which tracks the status of contracting officer actions on Defense Contract Audit Agency (DCAA) reports. Our evaluation disclosed several instances where the CAFU data were inaccurate and did not comply with DoD Instruction 7640.02, "Policy for Follow-up of Contract Audit Reports," April 15, 2015. We conducted this evaluation in accordance with the Council of the Inspectors General on Integrity and Efficiency "Quality Standards for Inspection and Evaluation."

We considered management comments on a draft of this report. DoD Instruction 7650.03 requires that recommendations be resolved promptly. Comments from the Director, Defense Contract Management Agency, were partially responsive for Recommendation 3.b. We request additional comments by June 13, 2016. Comments from the Director of DCAA conformed to the requirements of DoD Instruction 7650.03; therefore, we do not require additional comments from DCAA.

Please send a PDF file containing your comments to the e-mail address included in the last paragraph of this memorandum. Copies of your comments must have the actual signature of the authorizing official for your organization. We cannot accept the /Signed/ symbol in place of the actual signature. If you arrange to send classified comments electronically, you must send them over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Please direct questions to Ms. Carolyn R. Hantz at (703) 604-8877, or e-mail at [carolyn.hantz@dodig.mil](mailto:carolyn.hantz@dodig.mil).

  
Randolph R. Stone  
Deputy Inspector General  
Policy and Oversight

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## Acronyms and Abbreviations

# Introduction

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## Objective

Our objective was to evaluate the accuracy of data residing in the Contract Audit Follow-Up (CAFU) System. DoD Components use CAFU to report on contracting officer actions taken in response to Defense Contract Audit Agency (DCAA) audit reports. The accuracy of CAFU is important to effectively document and monitor contracting officer actions on DCAA reported audit findings.

As part of our evaluation, we randomly selected 50 CAFU records that Defense Contract Management Agency (DCMA) contracting officers dispositioned<sup>1</sup> between April 1, 2014 and September 30, 2014. See the Appendix for a discussion of our scope and methodology. Although all DoD Components use CAFU, we focused our evaluation on the accuracy of CAFU records assigned to DCMA contracting officers because DCMA is responsible for taking action on most DCAA audit reports.

## Background

### ***Defense Contract Audit Agency***

DCAA performs contract audits for DoD. DCAA operates in accordance with DoD Directive 5105.36, "Defense Contract Audit Agency," January 4, 2010, and reports to the Under Secretary of Defense (Comptroller)/Chief Financial Officer. It performs several types of contract audits, such as audits of a DoD contractor's proposed incurred costs, business systems, and compliance with the Cost Accounting Standards. During FY 2014, DCAA audit reports questioned \$10.7 billion in proposed DoD contractor costs.

### ***Defense Contract Management Agency***

DCMA is a DoD Component that works directly with DoD contractors to ensure that DoD, Federal, and allied Government supplies and services are delivered on time and at projected cost. DCMA contracting officers are responsible for several contract administrative functions such as approving or disapproving contractor business systems, determining final indirect cost rates on cost-reimbursement

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<sup>1</sup> "Dispositioned" refers to the status of an audit report when the contracting officer has prepared a signed and dated post-negotiation memorandum and (i) the contracting officer has either made a final determination, negotiated a settlement, or taken final action, (ii) the ASBCA or U.S. Court of Federal Claims renders a decision and all required actions are complete and contractual documents are executed, or (iii) DCAA supplements or supersedes the audit report.

contracts, and evaluating contractor compliance with the Cost Accounting Standards. DoD Instruction 7640.02, "Policy for Follow-up on Contract Audit Reports, April 15, 2015,"<sup>2</sup> details the requirements and responsibilities for taking action on audit reports issued by DCAA.

### ***Department of Defense Instruction 7640.02***

The Instruction establishes record-keeping and reporting requirements for "reportable"<sup>3</sup> contract audits. In support of the record-keeping requirements, DCMA maintains an automated database (referred to as CAFU) that DoD Components use to track and record the actions taken to resolve and disposition reportable contract audits. DoD Component contracting officers (including DCMA contracting officers) must promptly update the status of their actions on DCAA reportable audit reports assigned to them in the CAFU system.

DoD Instruction 7640.02 also requires that DCAA send DCMA a list of new reportable audit reports issued each month for inclusion in CAFU (hereafter referred to as the "monthly report list"). For each report included in the monthly report list, DCAA furnishes specific information such as the report number, amount of questioned costs, amount of questioned costs subject to penalty, and whether the report includes qualifications<sup>4</sup> or unresolved<sup>5</sup> costs. DCAA uses its management information system (also known as DMIS) to prepare the monthly report list. DCMA uploads the list into CAFU after receiving it from DCAA.

DoD Instruction 7640.02 states that contracting officers must ensure the accuracy of CAFU data for audit reports assigned to them, including the data DCAA provides in its monthly report list, and promptly update the status of their actions in the CAFU system. Once they complete certain actions, contracting officers must enter key information in CAFU, such as the amount of questioned costs they sustain, the date they resolve<sup>6</sup> the audit report, and the date they disposition<sup>7</sup> the audit report.

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<sup>2</sup> The August 22, 2008, version of DoD Instruction 7640.02 applies to the CAFU reports we selected for evaluation. However, except where otherwise stated, the current April 15, 2015, version of DoD Instruction 7640.02 is consistent with the August 22, 2008, version for all significant matters discussed in this report and is the basis we cite for our findings and recommendations.

<sup>3</sup> With limited exceptions, DoD Instruction 7640.02 defines reportable contract audit reports as all contract audit reports that include questioned costs or recommendations and that require contracting officer action.

<sup>4</sup> DCAA qualifies its reported opinion when, at the time of report issuance, the auditor is unable to provide a definitive conclusion on the allowability, allocability, and reasonableness of the costs under examination.

<sup>5</sup> DCAA classifies a cost as unresolved when the cost is associated with an outstanding request for an audit being performed by another DCAA field office (also referred to as an "assist audit").

<sup>6</sup> A contracting officer resolves an audit report when they document an action plan for addressing the reported findings in a pre-negotiation memorandum.

<sup>7</sup> Disposition occurs when the contracting officer prepares a post-negotiation memorandum and completes any other necessary actions on the audit report.



***Semiannual Report to Congress***

The Inspector General Act of 1978, as amended, requires each inspector general to prepare semiannual reports to Congress summarizing the activities of the office during the immediately preceding 6-month periods ending March 31 and September 30. The DoD Inspector General Semiannual Report to Congress (SAR) includes an appendix (“Status of Action on Post-Award Contracts”) that provides a summary on the status of contracting officer actions on DCAA reportable audit reports. The DoD Inspector General uses information residing in CAFU to prepare the appendix.

## Finding

### Improvements Needed to Enhance the Accuracy of CAFU Records

Of the 50 CAFU records we tested, 41 had errors in 1 or more data fields. Each record includes up to 20 data fields. In total, 100 data fields had errors. The errors resulted from DCAA providing inaccurate audit information in its monthly report list, or DCMA contracting officers entering incorrect status information in CAFU. In the past, we found similar errors while compiling summary statistics from CAFU for inclusion in the SAR. Finally, DCAA lacks a procedure for notifying DCMA of corrections that need to be made for data residing in CAFU. The accuracy of CAFU is important to ensure reported DCAA audit findings are resolved timely and appropriately, and to correctly report the status of actions taken on the reported findings to Congress.

### Scope of Testing

We randomly selected 50 CAFU records to evaluate their accuracy. Each record includes up to 20 data fields containing information on each audit report and the status of actions that the assigned contracting officer has taken on the report. The number of data fields that apply for a given CAFU record varies depending on the type of audit report. For example, the “Questioned Cost” field applies to audits of DoD contractor incurred costs but not to audit reports of DoD contractor business systems.

For the 50 selected records, we focused our testing on 10 key data fields. Six of the 10 data fields are populated from the monthly report list that DCAA furnishes and DCMA uploads to CAFU. The remaining four data fields include status information that contracting officers enter in CAFU for each audit report assigned to them. We verified the accuracy of the tested data fields by comparing them to supporting documentation retained in DCAA audit files or DCMA contract files.

### Results of Testing

Of the 50 CAFU records we tested, 41 records (82 percent) contained inaccurate information in 1 or more data fields that make up each record. In total, 100 data fields had errors, all contained in 6 of the 10 key data fields tested. We did not find any errors in the remaining four data fields we tested, including the Contractor Name, Audit Type, Audit Report Date, and Penalty Assessed data fields. Table 1 depicts the number of errors we found within the six data fields (See Table 4 for the detailed results by CAFU record).

Table 1. CAFU Errors by Data Field

Six Data Fields With Errors	Results of CAFU Records Tested		
	CAFU Records Tested	CAFU Record Errors	Error Rate
Questioned Cost	28	10	36%
Qualifications or Unresolved Cost	50	18	36%
Questioned Cost Subject to Penalty	14	12	86%
Questioned Cost Sustained	28	15	54%
Resolution Date	50	22	44%
Disposition Date	50	23	46%
<b>Total Errors</b>		<b>100</b>	

### Questioned Cost

This field represents the amount of DCAA reported audit exceptions identified in the audit report. Of the 50 records we selected, 28 included an amount recorded in the “Questioned Cost” data field. Of the 28 Questioned Cost fields we tested, 10 had errors. For example, 1 CAFU record showed questioned cost of \$400,565, but the DCAA audit report had actually identified questioned cost of \$435,396. The 10 inaccuracies resulted in a \$2,624,658 overstatement of questioned cost within CAFU. Regarding the 10 errors, DCAA and DCMA did not comply with DoD Instruction 7640.02 for the following reasons:

- In three instances, DCMA added a CAFU record for a non-reportable audit.<sup>8</sup>
- In three instances, DCAA excluded questioned cost that was directly traceable to a specific contract.
- In one instance, DCAA excluded a downward adjustment to the questioned cost in its monthly report list.
- In one instance, DCAA reduced the questioned cost for government participation.
- In one instance, DCMA incorrectly adjusted the questioned cost that DCAA had accurately reported.
- In one instance, DCAA included questioned cost from an assist audit that was separately reported in CAFU.

<sup>8</sup> An audit exempt from the reporting requirements of DoD Instruction 7640.02, enclosure 3, paragraph 1.b.

### ***Qualifications or Unresolved Cost***

This data field denotes whether DCAA reported qualifications or unresolved costs within the DCAA audit report. DoD Instruction 7640.02 requires that the field state “Yes” if DCAA reported qualifications or unresolved costs, or “No” if DCAA did not. Of the 50 CAFU records, 18 (36 percent) did not accurately reflect whether DCAA had reported qualifications or unresolved costs, including:

- 6 fields that were left blank but a “No” was required;
- 6 fields that were left blank but a “Yes” was required;
- 4 fields that included a “No” but a “Yes” was required; and
- 2 fields that were populated for a non-reportable audit.

DCAA did not include the “Qualifications or Unresolved Cost” data field in its monthly report list. Instead, DCAA furnished an “Audit Opinion” field that reflected the type of opinion expressed in the audit report. For example, DCAA entered an “A” code for an adverse opinion, or a “D” code for a disclaimer of opinion. Although DCMA attempted to convert the audit opinion code to a “Yes” or “No” as DoD Instruction 7640.02 requires, the conversion process frequently resulted in errors.

In accordance with DoD Instruction 7640.02, DCAA needs to begin including the “Qualifications or Unresolved Cost” field in its monthly report list. The accuracy of this field will help to highlight any qualifications or unresolved costs that contracting officers must consider before they complete their actions on the audit report.

### ***Questioned Cost Subject to Penalty***

This field represents the amount of questioned cost that DCAA reported as expressly unallowable in accordance with Federal Acquisition Regulation (FAR) Subpart 31.205, “Selected Costs,” and subject to a penalty in accordance with FAR 42.709-3, “Assessing the Penalty.” Of the 50 records, 14 should have been populated with an amount in the “Questioned Cost Subject to Penalty” data field. We tested the 14 fields and found that 12 had errors because the CAFU data field did not agree with the actual questioned cost subject to penalty reported by DCAA. In total, the 12 errors resulted in CAFU understating the questioned cost subject

to penalty by \$11,026,909. DCAA furnishes the questioned cost subject to penalty in its monthly report list. For the 12 errors, DCAA or DCMA did not comply with DoD Instruction 7640.02 because:

- In seven instances, DCAA reduced the questioned cost subject to penalty to account for the percent of commercial business and contract type. DCAA policy allows for reporting of either the total amount or the reduced amount, contrary to DoD Instruction 7640.02.
- In two instances, DCAA included no questioned cost subject to penalty. DCAA policy prohibits the reporting of amounts less than \$10,000 (which is the threshold for waiving penalties established in FAR 42.709-5(b), “Waiver of the Penalty”).
- In one instance, DCAA did not include \$417,996 in questioned cost subject to penalty because it considered the amount immaterial after adjusting for the percent of commercial business.
- In one instance, DCAA mistakenly omitted the questioned cost subject to penalty.
- In one instance, DCMA mistakenly included questioned cost subject to penalty associated with a non-reportable audit.

DoD Instruction 7640.02 requires that questioned costs should not be reduced for the percent of commercial business or contract type. Also, the Instruction does not include a minimum value for reporting questioned cost subject to penalty in CAFU. DCAA should revise its procedures to ensure the accurate and consistent reporting of questioned cost subject to penalty in accordance with DoD Instruction 7640.02.

### ***Questioned Cost Sustained***

In accordance with DoD Instruction 7640.02, this data field reflects the questioned amounts that are agreed to by the contractor during the course of the audit, and those resulting from a contracting officer’s final decision. Contracting officers enter this amount in CAFU after completing all necessary actions on the audit report. Of 28 questioned cost sustained fields we tested, 15 had errors. The 15 errors resulted in CAFU overstating questioned cost sustained by \$8,377,829. The errors occurred because DCMA contracting officers did not comply with DoD Instruction 7640.02 for the following reasons:

- In three instances, contracting officers included questioned cost sustained for non-reportable audits.
- In two instances, contracting officers input the penalty amount in CAFU instead of the questioned cost sustained amount.

- In one instance, a contracting officer excluded questioned cost that the contractor agreed to during the audit.
- In one instance, a contracting officer did not adjust the “Questioned Cost Sustained” data field for the final amount established by a court order.
- In eight instances, for unknown reasons contracting officers entered an amount in CAFU that was inconsistent with the questioned costs actually sustained and documented in the negotiation memorandum. For example, one contracting officer reported in CAFU that he had sustained \$5 million in DCAA-reported questioned cost, but he had not yet taken any action on the questioned cost.

### ***Resolution/Disposition Dates***

DoD Instruction 7640.02 requires the contracting officer to resolve reported audit findings within six months, and complete the disposition of audit findings within 12 months. Contracting officers are responsible for accurately recording the resolution and disposition dates they enter in CAFU.

Of the 50 records in our sample, contracting officers entered 22 inaccurate resolution dates and 23 inaccurate disposition dates. The resolution dates were inaccurate by an average of 196 days, and the disposition dates were inaccurate by an average of 34 days. We noted the following reasons for the errors:

- Fourteen errors occurred when contracting officers entered resolution and disposition dates for non-reportable audits.
- Nine errors resulted from contracting officers entering resolution or disposition dates without completing all required actions. For example, in two instances contracting officers entered a disposition date but did not take action on \$254,347 in direct questioned cost (that is, questioned cost charged to one contract instead of an indirect cost pool).
- For the remaining 22 errors, the resolution and disposition dates recorded in CAFU did not agree with the actual dates documented in DCMA contract files. In these instances, we did not identify a specific reason for the errors.

### **Previous Questioned Cost Sustained Errors**

For the last four semiannual reporting periods, we found several questioned cost sustained errors that we corrected before issuing our SAR. The errors resulted from DCMA contracting officers entering questioned cost sustained that exceeded the DCAA-reported questioned cost. For one of the reporting periods, the errors could have caused a \$1.97 billion overstatement of questioned cost sustained

reported in the SAR. Table 2 summarizes the number of errors that we detected and had corrected in CAFU, thereby avoiding significant overstatements of questioned cost sustained in the SAR.

*Table 2. Detected Errors and Overstatement of Questioned Cost Sustained*

Reporting Period	(\$ in millions)			Percent Overstatement
	CAFU Questioned Cost Sustained	Actual Questioned Cost Sustained	Overstatement of Questioned Cost Sustained	
September 30, 2013	\$1,462	\$541	\$921	170%
March 31, 2014	2,429	463	1,967	425%
September 30, 2014	414	404	10	2%
March 31, 2015	1,370	408	962	236%
<b>Total</b>			<b>\$3,860</b>	

Although we detected and corrected the errors before issuing our SAR, DCMA needs to implement a control that will help prevent a contracting officer from entering in CAFU a questioned cost sustained amount that exceeds the DCAA-reported questioned cost.

## Previous Dispositions Did Not Address Direct Questioned Costs

DCMA contracting officers did not always take action on direct questioned cost reported by DCAA. While compiling data for the September 30, 2013, SAR, we found that DCMA contracting officers had dispositioned three records in CAFU but took no action on \$254 million in direct questioned cost. Generally, DCMA contracting officers negotiate only indirect questioned cost, and procurement contracting officers from other DoD Components negotiate any direct questioned cost. Nevertheless, before DCMA contracting officers can disposition the CAFU record, they must coordinate with procurement contracting officers that have negotiation responsibility of any direct questioned cost. DoD Instruction 7640.02, enclosure 3, states that contracting officers must:

- coordinate with other Government agencies that have responsibility for resolving a portion of the audit findings and recommendations;
- address all audit findings and recommendations (including the disposition of unresolved costs and the assessment of penalties and interest) and complete the post-negotiation memorandum before reporting the audit as “dispositioned” in CAFU; and
- incorporate the negotiation results from other Government agencies in the post-negotiation memorandum, if applicable.

In addition, DCMA Instruction 125, “Final Overhead Rates,” emphasizes that the DCMA contracting officer should coordinate with the procurement contracting officer having responsibility to resolve direct costs questioned by DCAA to help ensure the appropriate resolution of direct questioned cost.

When DCMA contracting officers disposition and close a record in CAFU before addressing all questioned cost, DoD management loses the ability to effectively monitor the contracting officer’s actions on the remaining questioned cost. Furthermore, the Government could lose its ability to recoup the remaining questioned cost if the contract is closed before the contracting officer takes action on the questioned cost.

### Previous Dispositions Were Not Included in the SAR

DCMA excluded 35 dispositioned audits in its reporting of dispositioned audits for the March 31, 2015, SAR. We did not detect the excluded audits before we issued the SAR, resulting in a significant understatement of reported questioned cost and questioned cost sustained. DCMA stated a programming error caused the understatement, but that the Agency has since corrected it. DCMA also stated that it has implemented controls to help prevent any reoccurrence. Table 3 depicts the understatement of questioned cost and questioned cost sustained for the 35 dispositioned audits.

Table 3. Understatement of CAFU Information in the SAR for Period Ended March 31, 2015

Reported Information	(in millions)			Percent Understatement
	Reported Amount	Actual Amount	Understated Amount	
Questioned Cost	\$1,271	\$1,361	\$90	7%
Cost Sustained	408	432	24	6%

We will include an explanatory note on the error in the March 31, 2016, SAR. Finally, we did not evaluate the DCMA corrective actions as part of this evaluation. We may assess DCMA’s corrective action during a future evaluation.

### DCAA Has No Procedure for Notifying DCMA of Monthly Report List Errors

DCAA does not have a procedure for notifying DCMA of errors that DCAA discovers after the monthly report list is uploaded to CAFU. DCAA uses its management information system to generate the monthly report list. Occasionally, DCAA will discover and correct errors in its management information system, but because DCAA does not typically notify DCMA of the errors, they may not be corrected in CAFU.



Inaccurate CAFU records diminish the reliability of CAFU as a management tool and can materially misstate the CAFU information reported in the SAR. DCAA should implement procedures for ensuring that any errors discovered by DCAA are communicated to DCMA and corrected in CAFU.

## Conclusion

Of the 50 CAFU records we tested, 41 (82 percent) contained errors within 1 or more data fields. The errors resulted from DCAA providing inaccurate audit report data in its monthly report list, or from DCMA contracting officers entering inaccurate status information in CAFU. We have noted previous CAFU errors while compiling data for the SAR. CAFU data errors impact:

- the reliability of the system as a tool for documenting contracting officer actions on DCAA audit findings,
- DoD Component management's ability to effectively monitor the status of actions on DCAA audit reports, and
- the accuracy of data reported in the SAR.

The frequency of the CAFU errors demonstrates the need to improve the associated procedures and internal controls. To improve CAFU accuracy, DCAA and DCMA should provide refresher training and modify certain procedures to comply with the DoD Instruction 7640.02 reporting requirements.

## Recommendations, Management Comments, and Our Response

### ***Recommendation 1***

**We recommend that the Directors, Defense Contract Audit Agency and Defense Contract Management Agency provide refresher training on DoD Instruction 7640.02 reporting requirements to employees involved in Contract Audit Follow-up reporting, with emphasis on accurately:**

- Classifying audit reports as “reportable” or “not reportable.”**
- Reporting questioned cost, qualifications or unresolved cost, questioned cost subject to penalty, questioned cost sustained, and resolution and disposition dates.**

### ***Director, Defense Contract Audit Agency, Comments***

The Director, DCAA, agreed and stated that the Agency will provide refresher training to its employees on the CAFU reporting requirements. The training will include criteria for differentiating between “reportable” and “not reportable” audits and instructions for helping to ensure CAFU data accuracy. DCAA will complete the training by December 2016.

*Director, Defense Contract Management Agency, Comments*

The Director, DCMA, agreed and has changed DCMA Instruction 126, “Contract Audit Follow Up (CAFU),” to be consistent with DoD Instruction 7640.02. The changes were implemented in February 2016 and address the definitions of reportable and non-reportable audit reports. In addition, DCMA provided training sessions in March 2016 on the recent revisions to DoD Instruction 7640.02. The training emphasized that contracting officers should avoid adding records in CAFU to reduce reporting errors. The DCMA training also emphasized the definitions of the “Questioned Cost” and “Questioned Cost Sustained” data fields.

*Our Response*

Comments from the Directors of DCAA and DCMA addressed the specifics of the recommendation, and no additional comments are required. Once completed, we request that DCAA provide evidence of the training provided to its employees on the CAFU reporting requirements.

As part of DCMA’s management comments, DCMA included a copy of revised DCMA Instruction 126 and evidence of training. Therefore, we do not require any additional information from DCMA on Recommendation 1.

**Recommendation 2**

**We recommend that the Director, Defense Contract Audit Agency modify Agency procedures and related internal controls to:**

- a. Accurately classify audits as reportable or not reportable in the monthly report list that DCMA uploads to the Contract Audit Follow-up System.**

*Director, Defense Contract Audit Agency, Comments*

The Director, DCAA, agreed and stated that the errors occurred because DCAA staff input inaccurate information in its management information system. DCAA will provide training to its staff, which will address the criteria for “reportable” and “not reportable” audits. DCAA will complete the training by December 2016.

*Our Response*

Comments from the Director, DCAA, addressed the specifics of the recommendation, and no additional comments are required. Once completed, we request evidence of the training provided to DCAA staff.

- b. Include the “Qualifications or Unresolved Cost” data field in the Defense Contract Audit Agency monthly report list of reportable audits, as DoD Instruction 7640.02, enclosure 4, paragraph 2.j requires.**

*Director, Defense Contract Audit Agency, Comments*

The Director, DCAA, agreed in principle. DCAA will work jointly with DCMA to develop a corrective action plan that will help ensure compliance with DoD Instruction 7640.02, paragraph 2.j. DCAA will complete its corrective actions by September 2016.

*Our Response*

Comments from the Director, DCAA, addressed the specifics of the recommendation, and no additional comments are required. Once developed, we request that DCAA furnish us with a copy of the corrective action plan for ensuring compliance with DoD Instruction 7640.02.

- c. Report all questioned cost subject to penalty regardless of dollar value, which are not reduced for percent of commercial business or contract type as DoD Instruction 7640.02, enclosure 3, paragraph 1.b.(4)(d)4 specifies.**

*Director, Defense Contract Audit Agency, Comments*

The Director, DCAA, agreed and stated that DCAA will remove the \$10,000 minimum limitation from its management information system. In addition, DCAA will change its guidance to state that the reported questioned subject to penalty should not be reduced. DCAA will complete the corrective actions by May 2016.

*Our Response*

Comments from the Director, DCAA, addressed the specifics of the recommendation, and no additional comments are required. We request that DCAA provide us with evidence of the completed corrective actions.

- d. Notify the Defense Contract Management Agency of significant corrections made to contract audit follow-up information previously included in the Defense Contract Audit Agency monthly report list.**

*Director, Defense Contract Audit Agency, Comments*

The Director, DCAA, agreed and stated that DCAA will implement procedures to alert DCMA of any significant corrections to previously reported CAFU information. Initially, DCAA will inform DCMA of the changes separate from its transmission of the CAFU monthly report list. DCAA will coordinate with DCMA and make any modifications necessary to ensure that accurate CAFU information is not overwritten in error. DCAA will complete the corrective actions by March 2017.

*Our Response*

Comments from the Director, DCAA, addressed the specifics of the recommendation, and no additional comments are required. Once completed, we request that DCAA provide us with evidence of the corrective actions.

***Recommendation 3***

**We recommend that the Director, Defense Contract Management Agency modify Agency procedures and related internal controls to help:**

- a. Prevent contracting officers from entering a Cost Questioned Sustained amount in the Contract Audit Follow-up System that exceeds the Defense Contract Audit Agency-reported questioned cost.**

*Director, Defense Contract Management Agency, Comments*

The Director, DCMA, agreed with the recommendation. On March 16, 2016, DCMA implemented a software modification to preclude contracting officers from closing a record with a “sustained amount” that is inconsistent with the DCAA questioned cost.

*Our Response*

Comments from the Director, DCMA, addressed the specifics of the recommendation, and no additional comments are required. We request that DCMA provide us with evidence on effectiveness of the software modification.

- b. Ensure that contracting officers complete their required actions on all Defense Contract Audit Agency findings before they record the audit report as “dispositioned” in the Contract Audit Follow-up System.**

*Director, Defense Contract Management Agency, Comments*

The Director, DCMA, agreed in part. DCMA will update DCMA Instruction 126 to require that the DCMA contracting officer contact the procurement contracting officer with authority to settle direct cost to ensure the procurement contracting officer 1) received the DCAA audit report, 2) understands the audit findings, and 3) knows how the findings impact the procurement contracting officer’s contracts. Once accomplished, the updated Instruction will allow the DCMA contracting officer to close the CAFU record when all indirect costs and any direct costs for contracts administered by DCMA are settled. DCMA will complete the update by August 2016.

*Our Response*

Comments from the Director, DCMA, partially addressed the recommendation. DCMA’s planned update of DCMA Instruction 126 will make it inconsistent with DoD Instruction 7640.02. Specifically, allowing DCMA contracting officers to close a record before all reported questioned costs and recommendations are addressed would not comply with DoD Instruction 7640.02, enclosure 3, paragraph 3.b.(3), which requires that contracting officers address all reported findings and recommendations before they change a CAFU record to “dispositioned” and close it.

The update would also not comply with DoD Instruction 7640.02, enclosure 3, paragraph 3.b.(2), which requires the contracting officer to “incorporate the negotiation results from other government agencies in the post-negotiation memorandum, if applicable,” before dispositioning the CAFU record.

CAFU is an important tool used by DoD Components to track the status of contracting officer actions on DCAA audit findings. Once an audit report is closed in CAFU, DoD’s ability to effectively monitor a contracting officer’s actions on significant DCAA questioned costs (often valued in the millions of dollars) is diminished. As previously noted, we found three instances when contracting officers closed CAFU records but took no action on \$254 million in questioned direct costs.

Each CAFU record represents an individual DCAA audit report. Each audit report may address multiple contracts and, in most cases, CAFU assigns responsibility of each CAFU record to the primary DCMA contracting officer granted with administrative contract authority and responsibility for taking action on the report. We recognize the DCMA contracting officer assigned to the CAFU record may not be delegated the authority to settle DCAA questioned direct costs on all contracts covered in the audit report. The CAFU system, which DCMA is responsible for maintaining, does not have the ability to assign a CAFU record to multiple contracting officers.

Although DCMA contracting officers may not have the authority to negotiate direct questioned costs on all contracts, they normally are delegated the administrative responsibility and authority to approve final vouchers and close DoD contracts assigned to DCMA for administration. DCMA contracting officers assigned responsibility for CAFU records need to ensure that all DCAA questioned costs have been addressed before contract closeout. Otherwise, the DoD loses its ability to later recoup any questioned costs that the DoD contractor should not have billed under the DoD contract.

Therefore, we request that DCMA provide additional comments on the recommendation in response to the final report. DCMA's plan for allowing contracting officers to close a CAFU record before all questioned costs have been addressed would not comply with DoD Instruction 7640.02. This aspect of the update would also be contrary to DoD's interest in ensuring that contracting officers appropriately address all audit findings.

## Appendix

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### Scope and Methodology

We conducted this evaluation from March 2015 through January 2016 in accordance with the Council of the Inspectors General on Integrity and Efficiency “Quality Standards for Inspection and Evaluation.” As part of the evaluation, we randomly selected 50 of 687 DCAA reportable audit reports that DCMA dispositioned between April 2014 and September 2014. To accomplish our objective, we:

- gained an understanding of the data fields within the 50 DCAA reportable audit report records we selected for testing;
- interviewed appropriate DCMA and DCAA employees;
- analyzed DCAA audit files and DCMA contract files to verify the accuracy of the tested data fields;
- determined if the tested data fields were accurate and consistent with DoD Instruction 7640.02 (August 22, 2008, version) reporting requirements; and
- evaluated the effectiveness of the DCAA and DCMA procedures and related internal controls for helping to ensure compliance with DoD Instruction 7640.02.

### Use of Computer-Processed Data

We selected our sample of CAFU records based on a CAFU-generated list of audits dispositioned between April 1, 2014, and September 30, 2014. We verified the accuracy of the selected CAFU records by comparing them to appropriate documents contained in DCAA audit files and DCMA contract files. We did not test the list for completeness. However, it did not impact our results of the 50 records.

### Use of Technical Assistance

The DoD Office of Inspector General’s Quantitative Methods Division assisted us in selecting a cross section of 50 CAFU records for evaluation.

### Prior Report Coverage

We have not reported on the accuracy of CAFU during the last 5 years.

Table 4. CAFU Records with Errors (41)<sup>2</sup>

	CAFU Record/DCAA Report No.	CAFU Data Fields					
		Questioned Cost	Qualifications or Unresolved Cost	Questioned Cost Subject to Penalty	Questioned Cost Sustained	Resolution Date	Disposition Date
1	1241-2007J10100006			X		X	
2	1241-2008J10100006	X		X		X	
3	1281-2005A10100085	X		X			
4	1621-2014C17741014		X				
5	1701-2006X10100492			X	X		
6	1701-2012A19200003						X
7	1791-2007D10100007		X		X		
8	1791-2008B10100003			X			
9	2151-2007M10100031		X		X	X	X
10	2161-2007P10100024			X	X	X	
11	2171-2007N10100011 <sup>1</sup>					X	X
12	3121-2007110100022-S1			X			
13	3141-2007B10100011		X	X	X		
14	3161-2008A10100015	X	X		X		X
15	3171-2012T11070005					X	X
16	3231-2011L24010006		X			X	X
17	3311-2013J17900002 <sup>1</sup>	X			X	X	X
18	3321-2012N19500002						X
19	3531-2010B17740004		X				
20	3701-2012B19200001						X
21	3911-2008C10100024 <sup>1</sup>	X	X	X	X	X	X
22	4141-2007D10100001	X		X	X		



Table 4. CAFU Records with Errors (41)<sup>2</sup> (cont'd)

	CAFU Record/DCAA Report No.	CAFU Data Fields					
		Questioned Cost	Qualifications or Unresolved Cost	Questioned Cost Subject to Penalty	Questioned Cost Sustained	Resolution Date	Disposition Date
23	4261-2009C10100020		X				
24	4281-2006T10100004	X	X		X	X	X
25	4421-2007B10100001	X			X	X	X
26	4531-2011S24010004		X				X
27	4601-2008Y19200001					X	
28	4601-2013S17750001					X	
29	4721-2010A11010001		X				
30	4901-2010K17740001					X	X
31	4911-2006B10100006				X	X	X
32	6151-2006F10100024-S1		X	X	X		
33	6151-2007F10100057						X
34	6151-2009T10100057 <sup>1</sup>		X			X	X
35	6331-2006L10100039 <sup>1</sup>					X	X
36	6501-2006I10100001		X			X	X
37	9811-2008D10100001 <sup>1</sup>	X			X	X	X
38	9821-2007C10100001	X	X	X	X	X	X
39	9821-2014A23000004 <sup>1</sup>					X	X
40	9851-2007A10100008		X				X
41	9891-2010T17100001		X			X	
	<b>Total</b>	<b>10</b>	<b>18</b>	<b>12</b>	<b>15</b>	<b>22</b>	<b>23</b>

<sup>1</sup> Non-reportable audit report.<sup>2</sup> Table 4 excludes the remaining 9 records that contained no errors.

# Management Comments

## Defense Contract Audit Agency



**DEFENSE CONTRACT MANAGEMENT AGENCY**  
3901 A AVENUE, BUILDING 10500  
FORT LEE, VA 23801-1809

**MAR 31 2016**

MEMORANDUM FOR DEPARTMENT OF DEFENSE, DEPUTY INSPECTOR GENERAL,  
POLICY AND OVERSIGHT

SUBJECT: DCMA Comments to DoD IG Draft Report – “Evaluation of the Accuracy of Data  
in the DoD Contract Audit Follow-Up System,” dated March 2, 2016 (Project No.  
D2016-DAPOCF-0005.001)

The attached is in response to the subject DODIG draft report dated March 2, 2016 that  
addresses Recommendations 1 and 3 of the subject report.

The point of contact for this response is Ms. Joan Sherwood, at (804) 416-9062 or  
[joan.sherwood@dcma.mil](mailto:joan.sherwood@dcma.mil).

*Wendy M. Masiello*  
Wendy M. Masiello, Lt Gen, USAF  
Director

Attachment:  
As stated

## Defense Contract Audit Agency (cont'd)

OIG Draft Report Project No. D2016-DAPOCF-0005.001, "Evaluation of the Accuracy of Data in the DoD Contract Audit Follow-Up System," March 2, 2016

*Recommendation 1: We recommend that the Directors, Defense Contract Audit Agency and Defense Contract Management Agency provide refresher training on DoD Instruction 7640.02 reporting requirements to employees involved in Contract Audit Follow-up reporting, with emphasis on accurately:*

- a. Classifying audit reports as "reportable" or "not reportable."*
- b. Reporting questioned cost, questioned cost sustained, and resolution and disposition dates.*

### **JOINT RESPONSE:**

The Directors agree with the draft audit report recommendations (awaiting DCAA's response to recommendation 1).

On February 11, 2016, we issued an Immediate Policy Change (IPC) to the DCMA Instruction 126, "Contract Audit Follow Up (CAFU)." This IPC includes changes to DCMA practices to reflect the revisions to the DODI 7640.02, "Policy for Follow Up on Contract Audit Reports," dated April 15, 2015. The change in definitions of reportable and non-reportable audit reports will greatly improve the accuracy of the CAFU records. All audit reports with cost questioned audit findings or recommendations will now be considered reportable, with three simple exceptions. In addition to updates based on the revised DODI, we emphasized the importance of not entering other forms of audit correspondence into the Contract Audit Follow Up (CAFU) reporting records. The IPC is provided as attachment 1.

In concert with our release of DCMA INST 126 (IPC) for Contract Audit Follow Up, we gave training sessions on all the changes in the DODI 7640.02 and emphasized that manual entry of CAFU records should be avoided to reduce reporting errors. In addition, emphasis was provided on the definition of Questioned Costs (Updated) and question costs sustained. Resolution and Disposition dates are clearly defined in our DCMA INST 126. The sessions were provided on March 2nd, 3rd, and 8th 2016. The sessions were presented over eConnect and we recorded a total of 594 active data lines during the three sessions. The training slides are provided as attachment 2.

*Recommendation 3: We recommend that the Director, Defense Contract Management Agency modify Agency procedures and related internal controls to help:*

- a. Prevent contracting officers from entering a Cost Questioned Sustained amount in the Contract Audit Follow-up system that exceeds the Defense Contract Audit Agency-reported questioned cost.*
- b. Ensure that contracting officers complete their required actions on all Defense Contract Audit Agency findings before they record the audit report as "dispositioned" in the Contract Audit Follow-up System.*

## Defense Contract Audit Agency (cont'd)

OIG Draft Report Project No. D2016-DAPOCF-0005.001, "Evaluation of the Accuracy of Data in the DoD Contract Audit Follow-Up System," March 2, 2016

**DCMA RESPONSE:**

We agree with the draft audit report recommendation 3.a. We implemented a software modification to the Contract Audit Follow Up (CAFU) eTool on March 16, 2016 to preclude closing a record that includes a "sustained amount" inconsistent with questioned costs.

We agree in part with the draft audit report recommendation 3.b.

DCMA will update the DCMA INST 126, Contract Audit Follow Up (CAFU), to address the ACOs responsibilities for the resolution and disposition of audit findings within their control and document the file accordingly. The instruction update will require ACOs to contact the PCOs with administrative authority (when the PCO can be identified and located) to settle direct costs. ACOs are to ensure the PCO has received the audit report, understands the audit findings, and how the findings impact their contracts. Once this has been accomplished and documented, the ACO may proceed to close the record providing all the indirect costs and any direct costs for contracts we administer are settled. This update will be completed by August 30, 2016.

## Defense Contract Management Agency



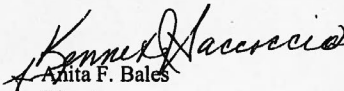
**DEFENSE CONTRACT AUDIT AGENCY**  
8725 JOHN J. KINGMAN ROAD, SUITE 2135  
FORT BELVOIR, VA 22060-6219

March 31, 2016

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR POLICY AND  
OVERSIGHT, OFFICE OF THE INSPECTOR GENERAL,  
DEPARTMENT OF DEFENSE

SUBJECT: Response to Office of Inspector General, Department of Defense, Report on  
Evaluation of the Accuracy of Data in the DoD Contract Audit Follow-Up System  
(Project No. D2016-DAPOCF-0005.001)

Thank you for the opportunity to respond to the subject draft report. We concur with  
your recommendations and will implement corrective actions as detailed in the Enclosure.

  
Anita F. Bales  
Director

Enclosure: a/s

## Defense Contract Management Agency (cont'd)

OIG Draft Report Project No. D2016-DAPOCF-0005.001, "Evaluation of the Accuracy of Data in the DoD Contract Audit Follow-Up System." March 2, 2016

**RECOMMENDATION 1: We recommend that the Directors, Defense Contract Audit Agency and Defense Contract Management Agency provide refresher training on DoD Instruction 7640.02 reporting requirements to employees involved in Contract Audit Follow-up reporting, with emphasis on accurately:**

**a. Classifying audit reports as "reportable" or "not reportable."**

DCAA Response: Concur. DCAA will provide the field refresher training on the Contract Audit Follow-Up Reporting requirements. The Training will include criteria for differentiating between "reportable" and "not reportable" assignments. This will be completed by December 2016.

**b. Reporting questioned cost, qualifications or unresolved cost, questioned cost subject to penalty, questioned cost sustained, and resolution and disposition dates.**

DCAA Response: Concur. DCAA will evaluate the errors noted in this report and develop training for the field to ensure the accuracy of CAFU reporting in the system. This will be completed by December 2016.

**RECOMMENDATION 2: We recommend that the Director, Defense Contract Audit Agency modify Agency procedures and related internal controls to:**

**a. Accurately classify audits as reportable or not reportable in the monthly report list that DCMA uploads to the Contract Audit Follow-up System.**

DCAA Response: Concur. DCAA uses criteria to identify reports that are reportable in accordance with DoD Instruction 7640.2. The errors identified were included because the Total Exception Dollar field in DMIS was incorrect, and not with the criteria for reporting. The April 2015 update to the instruction removed the dollar limitations on reportable assignments. As part of its training to its staff, DCAA will identify the criteria for differentiating between "reportable" and "not reportable" assignments. The training will also place an emphasis on calculating Total Exception Dollars in accordance with the instruction. This will be complete by December 2016.

**b. Include the "Qualifications or Unresolved Cost" data field in the Defense Contract Audit Agency monthly report list of reportable audits, as DoD Instruction 7640.02, enclosure 4, paragraph 2.j requires.**

DCAA Response: Concur in principle. The current data in our system may meet the intent of the Instruction. We will work jointly with DCMA to ensure our Agencies properly address the requirements of the DoD instruction related to paragraph 2.j and avoid any future errors in reporting. This will be completed by September 2016.

**c. Report all questioned cost subject to penalty regardless of dollar value, which are not reduced for percent of commercial business or contract type as DoD Instruction 7640.02, enclosure 3, paragraph 1.b.(4)(d)4 specifies.**

Enclosure  
Page 1 of 2

## Defense Contract Management Agency (cont'd)

OIG Draft Report Project No. D2016-DAPOCF-0005.001, "Evaluation of the Accuracy of Data in the DoD Contract Audit Follow-Up System." March 2, 2016

DCAA Response: Concur. DCAA will remove the \$10,000 limitation from its management information system and change the guidance to provide that the amount recorded should not be reduced for the participation of contracts subject to the penalty clause. This will be completed by May 2016.

**d. Notify the Defense Contract Management Agency of significant corrections made to contract audit follow-up information previously included in the Defense Contract Audit Agency monthly report list.**

DCAA Response: Concur. DCAA will implement procedures to identify significant changes to the contract audit follow-up information previously provided. Initially, those changes will be provided to DCMA outside of the current data transmission process. If the volume of changes justify modifying that process, the changes to the data transmission process will be coordinated between the agencies to ensure that prior accurate data is not overwritten by the automated process. This will be completed by March 2017.

Enclosure  
Page 2 of 2

## Acronyms and Abbreviations

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- CAFU** Contract Audit Follow-Up System
- DCAA** Defense Contract Audit Agency
- DCMA** Defense Contract Management Agency
- FAR** Federal Acquisition Regulation
- SAR** Semiannual Report



# **Whistleblower Protection**

## **U.S. DEPARTMENT OF DEFENSE**

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