

Inspector General

United States
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Internal Controls Over Payments Made in Iraq, Kuwait and Egypt

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Acronyms

CERP	Commander's Emergency Response Program
C.F.R.	Code of Federal Regulations
CPA	Coalition Provisional Authority
DCIS	Defense Criminal Investigative Service
DFARS	Defense Federal Acquisition Regulation Supplement
DFAS	Defense Finance and Accounting Service
DoD FMR	DoD Financial Management Regulation
DSSN	Disbursing Station Symbol Number
FAR	Federal Acquisition Regulation
OMB	Office of Management and Budget
PPA	Prompt Payment Act
SF	Standard Form
SIGIR	Special Inspector General for Iraq Reconstruction
U.S.C.	United States Code
USD/AT&L	Under Secretary of Defense for Acquisition, Technology, and Logistics
USD(C)/CFO	Under Secretary of Defense (Comptroller)/Chief Financial Officer



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May 22, 2008

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

SUBJECT: Report on Internal Controls Over Payments Made in Iraq, Kuwait, and Egypt
(Report No. D-2008-098)

We are providing this report for review and comment. We considered management comments on a draft of this report in preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. We request that the Under Secretary of Defense (Comptroller)/Chief Financial Officer provide additional comments on Recommendations A.2., C.1., C.2., and C.3. In addition, we request that the Assistant Secretary of the Army (Financial Operations) provide additional comments on Recommendation A.3. Management should provide comments on the final report by July 22, 2008.

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

We appreciate the courtesies extended to the staff. Questions should be directed to Mr. Jack L. Armstrong at (317) 510-4801, extension 274 (DSN 699-4801) or Mr. Craig W. Michaels at (317) 510-4801, extension 230 (DSN 699-4801). See Appendix G for report distribution. The audit team members are listed inside the back cover.

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Department of Defense Office of Inspector General

Report No. D-2008-098

May 22, 2008

Project No. (D2006-D000FL-0208.000)

Internal Controls Over Payments Made in Iraq, Kuwait, and Egypt

Executive Summary

Background. Between April 2001 and June 2006, the Army made 183,486 commercial and miscellaneous payments, totaling \$10.7 billion, from 7 Army contingency disbursing stations in Iraq, Kuwait, and Egypt. The contingency disbursing stations sent the payment vouchers to the accounting office at the Defense Finance and Accounting Service (DFAS) site in Rome, New York. The Defense Criminal Investigative Service determined that there had been only a limited review of the completeness, accuracy, and propriety of these payment vouchers and that the potential existed for fraud, waste, and abuse. As a result, we reviewed the payment vouchers to determine whether internal controls over the payments supporting the Global War on Terror provided reasonable assurance that payments were properly supported and recorded.

Results and Management Comments. The DoD has committed significant resources to the Global War on Terror. The Under Secretary of Defense (Comptroller)/Chief Financial Officer (USD[C]/CFO) and DFAS should have been directly involved in supporting military finance operations. However, DoD did not have adequate guidance to support financial operations in a military contingency environment. DoD did not have adequate internal controls over funds disbursed by contingency disbursing stations. On May 16, 2008, the office of the USD(C)/CFO notified us that the DoD Financial Management Regulation, Volume 10, Chapter 8, was revised to provide guidance on commercial payment vouchers and supporting documents in contingency operations. The new guidance is posted on its website. This action and the recommendations in this report, coupled with other actions already underway in DoD, will improve DoD finance operations in the military contingency environment.

Finding A. Commercial Payments. The Army did not maintain adequate internal controls over commercial payments to ensure that they were properly supported. We reviewed all payment support documentation for compliance with 53 statutory and regulatory requirements. However, after taking into consideration the reasonableness of completing all 53 requirements when making a payment in a military contingency environment, we determined that 27 of those requirements were the minimum necessary information to support a payment and mitigate the risk of making erroneous payments. We determined that the remaining 26 criteria were necessary for compliance with laws and regulations but were not essential information to preclude an erroneous payment in a military contingency operation. As a result, we estimated that the Army made \$1.4 billion in commercial payments that lacked the minimum supporting documentation and information for a valid payment, such as certified vouchers, proper receiving reports, and invoices. Payments that are not properly supported do not provide the necessary assurance that funds were used as intended. In addition, we estimated that \$6.3 billion of commercial payments contained the 27 criteria needed to properly support a payment but did not comply with other statutory and regulatory requirements and were still missing

items such as taxpayer identification numbers, contact information, and payment terms. The USD(C)/CFO, the Assistant Secretary of the Army (Financial Management and Comptroller), and the Director, DFAS have initiated several actions to address the internal control deficiencies identified during this audit. The Army and DFAS are transferring disbursing operations for contract payments back to the U.S., and DFAS deployed vendor pay and military pay subject matter experts to Iraq and Kuwait. The Army and DFAS are issuing guidance regarding the minimum acceptable level of supporting documentation for a commercial payment, as well as implementing a voucher support checklist and metrics to measure compliance. The Army and DFAS are also providing in-theater scanning technology to facilitate the review of voucher support documentation. Army and DFAS are also taking actions to improve training of finance personnel.

We recommended that the Under Secretaries of Defense for Acquisition, Technology and Logistics (USD/AT&L) and Comptroller/Chief Financial Officer resolve the conflicts in the Office of Management and Budget regulation implementing the Prompt Payment Act regarding disbursement support requirements in military contingency operations. However, working to resolve this conflict should not preclude specifying in regulation what minimum information is needed to support a proper payment. We also recommended that the USD(C)/CFO consolidate guidance that cites the Federal Acquisition Regulation and DoD 7000.14-R, DoD Financial Management Regulation requirements to support commercial payments and to include addressing the minimum essential information needed to support a proper payment. We further recommended that the Assistant Secretary of the Army (Financial Management and Comptroller) review the 125 commercial payments that were not properly supported, ensure that deployed finance personnel are properly trained, and direct the finance personnel to verify completion of a commercial payment support checklist. We also recommended that the Assistant Secretary include the reported internal control deficiencies as material weaknesses in the Annual Statement of Assurance. We also recommended that the Assistant Secretary establish a formal agreement with the Director, DFAS clarifying responsibilities for proper accountability of commercial payment vouchers. Management either partially concurred or concurred with recommendations.

Finding B. Contingency Operations and the Prompt Payment Act. The DoD Financial Management Regulation and Defense Federal Acquisition Regulation Supplement did not contain guidance addressing procedures to be used in a military contingency environment. The Office of Management and Budget allowed the DoD discretion in establishing the scope of contingency operations when applying the Prompt Payment Act. However, DoD has not established procedures addressing contingency operations. In addition, DoD needs to obtain clarification on the intent of the Office of Management and Budget regulation. As a result, DoD personnel relied upon existing requirements of the DoD Financial Management Regulation and Defense Federal Acquisition Regulation Supplement for making and processing commercial payments in Iraq and Kuwait. We recommended that the USD/AT&L and USD(C)/CFO coordinate to obtain legal advice to determine the impact of contract clauses that require making interest payments for existing contracts in military contingency operations. On March 5, 2008, the DoD Office of General Counsel issued a legal opinion that stated “the Department has sufficient legal authority to pay interest penalties [or obtain early payment discounts] pending resolution of the regulatory [conflict].”

Finding C. Payments to Foreign Governments. DoD did not maintain a complete audit trail to facilitate transparency regarding \$1.8 billion of seized and vested assets payments made to Iraqi representatives to ensure that the funds were accounted for, audited, and used to assist the Iraqi people. In addition, DoD did not maintain a

complete audit trail over \$134.8 million in Commander's Emergency Response Program (CERP) payments made to representatives of foreign governments. As a result, DoD was unable to provide reasonable assurance that the seized and vested asset funds disbursed were fully used to assist the Iraqi people, as prescribed in Executive Order 13290. Also, DoD is unable to ensure that CERP funds provided to Coalition Partners have been used for their intended purposes. We recommended that USD(C)/CFO update the DoD Financial Management Regulation to specify the supporting documentation needed for seized and vested asset payments to foreign government representatives, require payment reconciliations, and address the use of Coalition Partners as paying agents. The Deputy Chief Financial Officer stated that: audit trail documentation should not include budget details and spending plans; all funds advanced to Coalition Partners are already required to be reconciled; and a waiver is required for all non-U.S. citizens acting as paying agents. A Presidential memorandum dated April 30, 2003, requires seized and vested Iraqi assets to be properly accounted for, audited, and used to assist the Iraqi people. However, without support for the accounting and use of seized and vested assets, such as spending plans and budgets, there was no audit trail to demonstrate that the funds were used in accordance with the Executive Order. In addition, the DoD Financial Management Regulation needs to be updated to require reconciliations for payments to Coalition Partners and waivers for non-U.S. citizens acting as paying agents. Only payments to the United Kingdom were being reconciled, and the waiver request and approval process is not currently defined in DoD regulations.

Finding D. Advanced Iraqi Funds. The U.S. Army Corps of Engineers retained \$5.7 million in advanced seized and vested Iraqi assets in a suspense account for 21 months and had not made these funds available to pay for Iraqi debt with the U.S. Government or for other Iraqi projects. Based on our recommendation, the Corps collaborated with USD(C)/CFO regarding the disposition of these funds so that they could be put to better use.

We request that management provide comments on the final report by July 22, 2008. See the Finding sections for discussion of management comments and the Management Comments section for the full text of the comments.

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Background

This audit is the result of a Defense Criminal Investigative Service assessment saying that there had been only limited review of the completeness, accuracy, and propriety of contingency payment vouchers and that there existed the potential for fraud, waste, and abuse. This report addresses the supporting documentation for payments made by Army contingency disbursing stations and the processes used by the Army and Defense Finance and Accounting Service (DFAS) to review payment information.

Contingency Payments. The DoD has committed significant resources to the Global War on Terror. Army contingency disbursing stations perform military finance and accounting functions, including military, travel, and commercial payments (contract or vendor payments). From April 2001 through June 2006, the Army made 183,486 commercial and miscellaneous payments totaling \$10.7 billion, originating from 7 contingency disbursing stations in Iraq, Kuwait, and Egypt. Table 1 provides the number of vouchers and total amounts paid by disbursing station symbol number (DSSN).

<u>DSSN</u>	<u>Location</u>	<u>Number of Vouchers</u>	<u>Value (in millions)</u>
5579	Iraq	14,124	\$ 945.2
8547	Iraq	42,473	889.1
8550	Iraq	26,670	933.9
8551	Kuwait	27,586	3,643.8
8589	Iraq	8,808	306.8
8748	Kuwait	62,193	3,984.1
8788	Egypt	1,632	21.1
Total		183,486	\$10,724.0

From this universe of payments, we selected a statistical sample of 789 payments totaling \$3.5 billion to review. Appendix B contains the sampling plan and results. As shown in Table 2, our sample of 789 payments contained 702 commercial payments and 87 noncommercial payments (Findings A and B). Noncommercial payments included transfer payments to the Iraqi ministries and Coalition Partners (Finding C), advances to the U.S. Army Corps of Engineers (Finding D), and casual payments.

<u>Payment Type</u>	<u>Number of Vouchers</u>	<u>Value (in millions)</u>
Commercial (Findings A and B)	702	\$1,485.4
Foreign Government (Finding C)	75	1,960.6
Advanced Iraqi Funds (Finding D)	3	20.1
Casual Payments*	9	0.1
Total	789	\$3,466.2

*The casual payments were adequately supported

Accounting for Contingency Payments. DFAS Rome, New York, is the accounting office for payments made by the contingency disbursing stations in Iraq and Kuwait. Once a day, the Army contingency disbursing stations transmit electronic files that contain the DD 2657 form, “Daily Statement of Accountability,” and an electronic file of disbursements to DFAS Rome.¹ DFAS Rome uploads the electronic file into the Standard Finance System in order to perform the accounting for the Army contingency payments. DoD 7000.14-R, DoD Financial Management Regulation (DoD FMR), volume 10 requires that the accounting office receive copies of payment vouchers, invoices, and receiving reports. Each week the contingency disbursing stations mail the original payment vouchers and all supporting documentation to DFAS Rome. DFAS Rome manually matches payment vouchers to the entries in the Standard Finance System file.

Disbursement Guidance. Section 3325, title 31, United States Code (U.S.C.) asserts that disbursing officers should only disburse money if a voucher has been certified by an authorized certifying officer. This statute further discusses the disbursing officer’s examination of a voucher to determine whether: it is in proper form; it has been certified and approved; and it has been computed correctly. The official certifying the voucher is responsible for the information on the voucher and supporting records.

The Federal Financial Management Improvement Act of 1996 requires that agencies comply with Federal accounting standards and Federal system requirements. The Office of Federal Financial Management, “Core Financial Systems Requirements,” states that audit trails are essential to providing support and must exist for recorded transactions.

The Federal Acquisition Regulation (FAR) and DoD FMR provide regulatory requirements that implement the public laws discussed above. Commercial payments should be supported by documents containing the essential data required in these statutes. The FAR Part 13, “Simplified Acquisition Procedures,” provides policies for the acquisition of supplies and services. In addition, the FAR Part 32, “Contract Financing,” lists the criteria required for a

¹ The purpose of the DD 2657 is to summarize all disbursements and collections made during the business day by the disbursing officer and all deputies, agents, and cashiers.

proper invoice and receiving report to support a payment. Appendix E provides further detail on statutory and regulatory compliance criteria to determine whether a payment was properly supported.

The DoD FMR defines financial management responsibility for DoD components. The DoD FMR also defines the requirements for supporting payments made to vendors and contractors. The DoD FMR, volume 10 specifically prescribes the policy for:

- ensuring that vendors or contractors are entitled to payment for materials and services delivered to the Government;
- ensuring timely disbursements to vendors or contractors; and
- preparing payment vouchers and keeping contract, disbursement, and accounting records complete and accurate.

The DoD FMR, volume 5 governs DoD disbursing policy by establishing standards, responsibilities, procedures, and liability for disbursing officers, certifying officers, and accountable officials throughout DoD. Appendix D provides further detail on disbursing guidance.

Objectives

Our overall audit objective was to determine whether internal controls over payments made in Iraq, Kuwait, and Egypt supporting the Global War on Terror provided reasonable assurance that payments were properly supported and recorded. See Appendix A for a discussion of the scope and methodology and Appendix C for prior coverage related to the objective.

Review of Internal Controls

We identified material internal control weaknesses related to payments made in Iraq, Kuwait, and Egypt in support of the Global War on Terror, as defined by DoD Instruction 5010.40, "Managers' Internal Control Program Procedures," January 4, 2006. The Army's internal controls did not ensure proper support for the commercial payments and that funds were used as intended. The Army should address these internal control deficiencies as material weakness in its Annual Statement of Assurance. Implementing Recommendations A.1 through A.4, B.1 through B.3, and C.1 through C.3, will improve the internal controls over the Army's payments made in military contingency operations. We will provide a copy of the report to the senior official responsible for internal controls over Army disbursements made during military contingency operations.

A. Commercial Payments

The internal controls over commercial payments made by seven Army contingency disbursing stations were inadequate for commercial payment support. This occurred because Army finance personnel did not ensure that payment voucher documentation was available and complete, and finance personnel were not adequately trained. In addition, Army and DFAS internal control responsibilities for commercial payments in contingency operations needed to be clearly defined. As a result, we estimated that the Army made \$1.4 billion in commercial payments that lacked the minimum documentation for a valid payment, such as properly prepared receiving reports, invoices, and certified vouchers. We also estimated that the Army made an additional \$6.3 billion of commercial payments that met the 27 criteria for payment but did not comply with other statutory and regulatory requirements. These other requirements included taxpayer identification numbers, contact information, and payment terms. Payments that are not properly supported do not provide the necessary assurance that funds were used as intended. In addition, inadequate audit trails for payments resulted in unreliable disbursement amounts reported in the Army management reports and DoD financial statements.

Commercial Payment Review

As of June 2006, 7 Army contingency disbursing stations made an estimated 149,327 payments for \$7.8 billion that did not meet all statutory or regulatory requirements.² (Appendix E lists the criteria used to evaluate each commercial payment voucher.) We based the estimated amount of commercial payments on a sample of 702 payments. Of the 702 commercial payments, 662 had errors in payment support documentation, and some had more than one error. There were 125 payments not supported by the minimum documentation and information, which includes properly prepared receiving reports, invoices, and certified vouchers. An additional 537 commercial payments had the minimum documentation required for payment but did not meet other documentation and information requirements, such as taxpayer identification number, method of disbursement, and contact information. Only 40 commercial payments contained no errors. These transactions occurred between April 2001 and June 2006. Our review of the 702 payments did not provide evidence that the supporting documentation for these commercial payments improved during this period. The results of our review are depicted in Figure 1.

² There is a rounding difference between the estimated \$7.8 billion in payments with discrepancies and the combined total of the payments either not meeting minimal support requirements or identified as supportable but noncompliant.

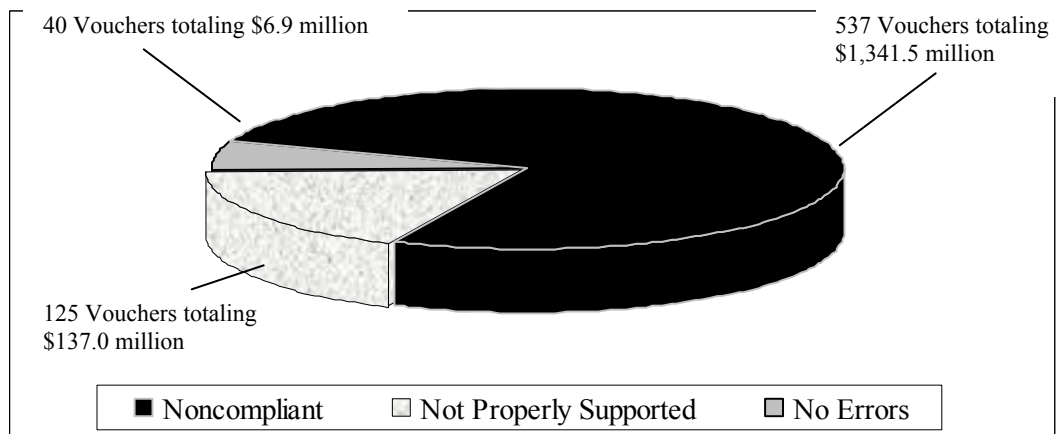


Figure 1. Voucher Review Results

Documentation Requirements. DoD had not specified adequate documentation requirements for disbursements made in a contingency environment. In November 2007, the DFAS Accounting Policy Office raised concerns that the Office of Management and Budget (OMB) in 5 Code of Federal Regulations (C.F.R.) Part 1315 (2001), which implements the Prompt Payment Act (PPA), has conflicting guidance related to documentation requirements for payments made in military contingency operations. 5 C.F.R. Part 1315, section 1315.5 states, “Payments made under a military contingency may be made as soon as the contract, proper invoice, receipt and acceptance documents or any other agreement are matched.” The FAR, Defense Federal Acquisition Regulation Supplement (DFARS), and DoD FMR implement these documentation requirements. However, Section 1315.5 appears to conflict with 5 C.F.R. Part 1315, section 1315.1, which states that vendor payments related to military contingency operations are exempt from the PPA. The FAR, DFARS, and DoD FMR do not address this exception or how it affects voucher documentation requirements in military contingency operations. As a result, Army finance personnel were required to follow existing documentation requirements prescribed in the FAR, DFARS, and DoD FMR. In addition, where PPA clauses were included in contracts, Army finance personnel were required to follow PPA documentation requirements prior to making payments. Finding B provides additional detail on the applicability of the PPA to military contingency operations.

We reviewed all payment support documentation for compliance with 53 statutory and regulatory requirements; however, only 27 of the requirements were necessary to support a payment and to reduce the risk of making erroneous payments. These 27 requirements are essential to support a payment in a military contingency operation. We determined that the remaining 26 criteria were necessary for proper compliance with laws and regulations but were not essential information to preclude an erroneous payment in a military contingency operation.

Minimum Documentation for Payment. The following examples came from our review of payment vouchers against the 27 criteria required to minimally support a commercial payment in a military contingency operation.

Receiving Report. Army finance personnel did not include documentation of the receipt of goods or services for 23 vouchers. According to the DoD FMR, volume 10, chapter 1 and FAR 32.905 “Payment Documentation Process,” all invoice payments must be supported by a receiving report. The DoD FMR, volume 10, chapter 8 states that vouchers should not be certified for payment before receipt of all supporting documents, including the receiving report. It also requires the disbursing office to review supporting documents on a periodic basis to ensure that those documents are available for review and to provide a copy of the receiving report to the accounting office. DFAS Rome is the accounting office for Army contingency disbursing stations. One voucher payment for \$11.1 million was missing both the receiving report and invoice. This payment was to a U.S. company; however, we could not identify the goods or services purchased. Without a receiving report, there is no evidence that the requesting organization received the goods or services purchased. In addition, because this voucher was also missing an invoice, it is unclear how the disbursing office determined that the vendor was entitled to payment or the amount that was due. The legitimacy of the payment is questionable given the absence of these supporting documents.

Invoice. Army finance personnel did not include vendor invoices supporting the amount paid for 23 vouchers. FAR 32.905 states that payments should be based on receipt of a proper invoice. The DoD FMR, volume 10, chapter 8 states that vouchers should not be certified for payment before receipt of all supporting documentation, including the invoice. It also requires that a copy of the invoice be provided to the accounting office. Like the \$11.1 million voucher discussed above, a voucher for a \$963,750 cash payment to a vendor was missing both the invoice and receiving report. As a result, we could not identify the goods or services purchased. The absence of needed information on the voucher, combined with the missing invoice and receiving report, prevented a determination of whether the vendor was legally entitled to payment.

Certifying Officer Signature. Army finance personnel paid five vouchers that were not certified for payment, three of which exceeded \$8 million. These three payments were to U.S. companies for vehicle rentals and support services. Section 3325, title 31, U.S.C.; Treasury Financial Manual, volume 1, part 4, chapter 2000; and the DoD FMR, volume 5, chapter 11 state that disbursing officers should approve payment only for vouchers that have been signed by an authorized certifying officer. The vouchers appeared to contain the necessary supporting documents, but should not have been paid because they were not properly certified. The certifying officer provides an important separation of duties function by ensuring that the goods or services received are correctly documented to entitle a payee to a disbursement of funds. The certification process also helps to ensure that payments are charged to the correct appropriation and are the correct amount. Payments made from uncertified vouchers should be reviewed for a potential loss of funds, for which the disbursing officer could be pecuniarily liable.

Payee Signature. Army finance personnel made cash payments on 15 vouchers totaling \$5.1 million to vendors without documentation showing payee signatures that the vendors actually received the cash. Three of the 15 vouchers were in excess of \$500,000. These payments were to a U.S.

company and two Iraqi companies for security services, trailers, and renovations. The DoD FMR, volume 5, chapter 11 requires the payee to sign the payment voucher upon receipt of cash. The payee's signature provides substantive evidence of receipt of the cash payment. Without the payee's signature, a disbursing officer may be unable to prove that proper payment was made and could be required to make the payment again.

Contract Number. Army finance personnel paid 31 vouchers that did not cite a contract number on the supporting invoice. One paid voucher with a missing contract number related to a \$3.3 million payment to a Jordanian company for bottled water. FAR 32.905 requires that payments be supported by a proper invoice containing the correct contract number. The contract number links other supporting documents in a voucher to the payment. Without the contract number on the invoice, errors could occur when attempting to match the payment with the correct contract or vendor.

Voucher Retention. The Army and DFAS could not locate two vouchers. One of the missing vouchers was for \$303,716. The DoD FMR, volume 5, chapter 11 requires all payments to be supported by a formal disbursement voucher. The DoD FMR, volume 5, chapter 21 states that original disbursing office records must be retained as Government property and remain accessible to the disbursing officer or designated settlement office for a period of 6 years and 3 months. Missing original vouchers should be reviewed to determine whether a loss of funds investigation is necessary.

Other Requirements. The following examples resulted from our review of payment vouchers compared against the 26 criteria identified as necessary for compliance with law and regulation. We did not consider these criteria to be essential to support a proper payment because they did not substantively relate to facts needed to determine entitlement.

Method of Disbursement. For 19 vouchers, Army finance personnel did not identify the method of disbursement. One of these was for an \$8.1 million payment for truck rentals. Disbursement method is required by the DoD FMR, volume 5, chapter 11. Specifically, the voucher should identify whether the method of disbursement was electronic funds transfer, U.S. Treasury check, or cash. Without the method of disbursement on the voucher, the audit trail for the payment becomes difficult to follow.

Printed Name on Receiving Report. Army finance personnel did not ensure that printed names of the approving officials were on receiving reports supporting 118 vouchers. One voucher with a receiving report that did not have the printed name of the approving official was for a \$19 million payment to a U.S. company for vehicle rentals. The FAR 32.905 requires a printed name. In addition, many signatures on the receiving reports were illegible. In some cases, we could not determine whether the mark on the receiving report was a signature. If there are questions regarding the goods or services received, the printed name is often the only way to identify the official who received or accepted the goods or services.

Use of the SF-44. Army finance personnel submitted 18 vouchers in which Standard Forms 44 (SF-44), “Purchase Order-Invoice-Voucher” were inappropriately used. The FAR Part 13 allows for the use of the SF-44 for on-the-spot, over-the-counter purchases with only one delivery and one payment. These 18 vouchers were supported by SF-44s used on a recurring basis or to make installment payments. In addition, Defense Federal Acquisition Regulation Supplement Subpart 213.306, “SF-44, Purchase Order-Invoice-Voucher” established that overseas transactions by contracting officers in support of a contingency operation cannot exceed the simplified acquisition threshold for using the SF-44. According to FAR Part 2, the simplified acquisition threshold for purchases made outside the United States is \$1 million. Because the guidance was fragmented, we had to research several sections of the FAR and DFARS regulations to determine which SF-44 purchase threshold applied to contingency operations.

In one instance, the Army incorrectly used an SF-44 to make a \$1.7 million installment payment on a contract for trucks. This payment did not meet the one-delivery and one-payment criteria and exceeded the simplified acquisition threshold for using the SF-44. The DoD FMR is required for use in day-to-day financial operations, but its explanation of the SF-44 is incomplete. Further, the DoD FMR refers only to FAR Part 13 for limitations and restrictions on the SF-44.

Contact Information on Receiving Report. For 394 vouchers, Army finance personnel did not ensure that the approving official’s contact information was included on the receiving report. One voucher with a receiving report that did not have approving official contact information was for a \$20.4 million payment to a U.S. company for vehicle rentals. The FAR 32.905 requires that a telephone number and mailing address for the approving official be included on the receiving report. Without ready contact information, it is more difficult for the certifying officer to contact the approving official to inquire about the receipt of goods or services. If voucher payment is delayed because of this, discounts for prompt payment could be lost.

Payment Terms. For 343 vouchers, the invoices did not state vendor payment terms. One voucher with an invoice missing the payment terms was for an \$8.2 million payment to a Kuwaiti company for food service. Payment terms define potential discounts from the vendor for payments made within a prescribed period. The FAR 32.905 requires that payment terms be included for a proper invoice. Stating payment terms on the invoice ensures that the disbursing office is aware of any potential discounts for early payment.

Contact Information on Invoice. For 359 vouchers, Army finance personnel did not require contact information on the vendor invoices. The FAR 32.905 requires the name, title, and phone number of a contact person to be on every invoice. In the event of a defective invoice, missing contact information could cause unnecessary delays, resulting in lost discounts from vendors or noncompliance with prompt payment requirements.

Taxpayer Identification. The taxpayer identification number was missing on 67 vouchers. Section 3325, title 31, U.S.C. and DoD FMR, volume 5,

chapter 11 require a taxpayer identification number on all certified vouchers submitted to a disbursing office for payment. Without the taxpayer identification number, the Internal Revenue Service is not notified when payment is made to a U.S. contractor. This could lead to the potential loss of tax revenue.

Commercial Payment Controls

Operating in a combat environment created challenges for Army contingency disbursing stations in ensuring good internal controls over the commercial payment process. The working relationship between DFAS Rome and Army disbursing stations for contingency commercial payments was not clearly defined in a formal plan or in guidance. As a result, neither DFAS Rome nor the Army disbursing stations had clear accountability for making proper contingency commercial payments or sufficiently defining the responsibilities for payment voucher retention.

In addition, the Army did not integrate its disbursing and accounting systems. This created problems in substantiating commercial payment transactions created at Army contingency disbursing stations. Currently, the contingency disbursing stations send daily text files of commercial payment data to DFAS Rome to populate the Standard Finance System, the Army-wide accounting system.

Each week, the contingency disbursing stations mail all original vouchers and supporting documents to DFAS Rome. DFAS Rome confirms that each payment voucher has a related transaction in the Standard Finance System. DFAS Rome completes a limited review of each payment voucher for certain required documents and data elements. This assessment does not include all the necessary payment elements required to properly support a commercial payment.

As a result, 125 of the 702 sample commercial payments did not have essential information needed to support a proper payment and 537 of the 702 sample commercial payments did not meet all the statutory and regulatory requirements. Four internal control deficiencies contributed to the Army's lack of compliance and should be addressed:

- availability of supporting documentation,
- payment voucher quality,
- training of Army finance personnel, and
- clarification of accountability for the Army and DFAS in the commercial payment process.

Management Actions. On May 16, 2008, the office of the USD(C)/CFO notified us that the FMR, Volume 10, Chapter 8, was revised to provide guidance on commercial payment vouchers and supporting documents in contingency operations. The revised guidance is posted to its website <http://www.defenselink.mil/comptroller/fmr>. Also, the Army and DFAS have implemented a number of process changes in response to the preliminary results

of this audit. These management actions should improve internal controls over commercial payments made by the Army contingency disbursing stations and reduce problems with payments in the future. The following sections discuss some of the Army and DFAS improvements.

Availability of Supporting Documents. Not all the information needed to support the sampled commercial payments was readily available at DFAS Rome, although the DoD FMR requires payment support vouchers and documents to be sent to the assigned accounting office. We reviewed the vouchers against 27 criteria developed from the statutory and regulatory requirements needed to minimally support a commercial payment. On May 3, 2007, we provided a memorandum to DFAS suggesting corrective actions and providing a list of major deficiencies identified in 152 commercial payment vouchers totaling \$167 million.³

The Army and DFAS were able to locate the necessary documents to support 27 of the 152 deficient commercial payments, totaling \$30 million. Supporting documentation was found in Iraq and Kuwait and at DFAS sites. However, critical information was still missing on 125 payment vouchers totaling \$137 million. We performed statistical analysis on our sample, which indicated that 34.2 percent of the universe of 183,486 commercial payments were not properly supported. Based on this, we estimate that the Army did not properly support 62,825 of the 183,486 commercial payments, for a total of \$1.4 billion. (See Appendix B for the details of the statistical analysis.) The Army should further review the 125 commercial payments that were not properly supported and, if they cannot be supported, determine whether a loss-of-funds investigation or other action is required to ensure that the payment was not improper. Other actions could include: referring unsupported payments to either the Defense Criminal Investigative Service or the U.S. Army Criminal Investigation Command or performing recovery audits of the payments.⁴

The Army and DFAS recently addressed the documentation problem by purchasing 40 scanners to be distributed to the Army contingency disbursing stations in Iraq and Kuwait. These disbursing stations will scan each day's disbursement documentation, and this input can be reviewed by DFAS Rome for document quality and completeness. Instead of shipping original disbursing documents to DFAS Rome each week, the Army will ship them only once per month. In light of this initiative by the Army and DFAS, we are not making any recommendations addressing the transfer and retention of disbursement voucher documentation.

In addition, DFAS Rome improved the physical controls over commercial payment vouchers and supporting documents by implementing the following:

³ DoD IG Memorandum, "Internal Payment Voucher Analysis Records from Audit of Internal Controls Over Out-of-Country Payments (Project No. D2006-D000FL-0208.000)," dated May 3, 2007.

⁴ DoD 7000.14-R, "DoD Financial Management Regulation," volume 10, chapter 22 defines a recovery audit as a post-payment review and analysis of the DoD Component's books, supporting documents, and other available information supporting its payments. Recovery audits are specifically designed to identify overpayments to contractors that are due to payment errors.

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- a single, dedicated storage area for all payment documentation,
 - restricted access to the storage area, and
 - strict procedures for checking out payment vouchers.

Completeness of Payment Documentation. Incomplete payment documentation resulted in part from inadequate quality assurance and management oversight. To correct these deficiencies, the Army and DFAS developed a checklist to use as a voucher review guide and established additional performance measures. In addition, the USD(C)/CFO has issued new guidance for certifying payments.

Checklist. DFAS Rome personnel addressed the problem of inadequate or missing payment support documents by developing internal procedures to process incoming vouchers. DFAS Rome had established a nine-item checklist to review some of the supporting documents and data elements required for a proper commercial payment. The checklist had served as a limited quality assurance review, and when a payment voucher needed to be corrected or lacked supporting documentation, DFAS Rome contacted the appropriate contingency disbursing station. However, the checklist lacked several statutory and regulatory requirements.

In our May 3, 2007, memorandum, we provided two additional recommendations to DFAS. We suggested that DFAS Rome should:

- expand its checklist to include the auditor-developed checklist of the 27 criteria needed to minimally support a payment, as well as those criteria required by regulation for otherwise-supported payments, and
- report to the Army the type and extent of errors in payment vouchers submitted to DFAS Rome.

In response, DFAS Rome staff stated that they had given a checklist of the 27 criteria needed to minimally support a commercial payment to the Army contingency disbursing stations for use in reviewing commercial payment vouchers. The Army should require certifying officers at all Army finance offices to complete a standard checklist of required commercial payment support elements before a payment voucher is forwarded to its appropriate disbursing and accounting office. This would ensure that all commercial payment vouchers are complete before they are sent to the appropriate accounting offices.

Performance Measures. The Army and DFAS Rome also added two new management performance indicators to evaluate payment support documents sent from Army contingency disbursing stations to DFAS Rome. These performance indicators were intended to ensure that the Army could assess a commercial payment voucher for completeness by evaluating the voucher's data elements against a new checklist developed by DFAS Rome. The indicators were based on the list of data elements developed by the Army and DFAS Rome, using the criteria needed to minimally support a commercial payment. However, the DFAS Rome checklist does not include verifying important specific information that should be included on certain payment support documents, such as specific

information that is required to be present on a receiving report or an invoice. The DFAS Rome checklist verifies only whether these documents are available and not whether they have the necessary specific information. Despite this, if these measures are fully and properly implemented, there should be a material improvement in the quality of incoming payment voucher documents from Army contingency disbursing stations. However, DFAS Rome will not have specific information to assess whether commercial payments are proper. As a result, Army contingency disbursing stations could still make payments that are not properly supported.

Under Secretary of Defense (Comptroller) Guidance. On September 14, 2007, the USD(C)/CFO issued a memorandum addressing “Certified Commercial Payments in Contingency Operations.” The purpose of the memorandum was to remind DoD components of the legal requirements for payment voucher certification and to provide guidelines for payments made in contingency operation areas. The 27 criteria that we identified as minimum essential information needed to support a proper payment complement this policy memorandum. The policy memorandum was in effect for 180 days. On May 16, 2008, the office of the USD(C)/CFO notified us that it had incorporated the memorandum guidance into the DoD FMR.

Training Army Disbursing Personnel. The Army had not provided adequate training on regulatory requirements for commercial payment support to Army finance personnel being deployed to contingency disbursing stations in Iraq and Kuwait. The Army does not currently offer any formal and up-to-date training in disbursing operations. In addition, the Soldier Support Institute stated that officers and enlisted personnel in finance do not currently receive a complete disbursing operations training course.

We interviewed 14 Army finance personnel in Iraq during May 2007. Half of them felt that they had not received sufficient disbursing and accounting training before their deployment. Some soldiers said that they had relied heavily upon their experience from previous deployments in Iraq because their training was not adequate. Active, Reserve, and National Guard finance soldiers deployed to Army contingency disbursing stations require sufficient training to perform their duties properly. Inadequate training has contributed to material errors in the preparation of documents supporting vendor and contractor payments.

To improve soldier preparation, the Soldier Support Institute is developing an on-line, computer-based disbursing operations course scheduled for deployment in mid calendar year 2008. This course will include lessons learned from soldiers with disbursing and finance experience in Iraq and Kuwait. In addition, DFAS Rome is taking a proactive role in training finance soldiers being deployed to Iraq and Kuwait. This training is held at DFAS Rome and Fort McCoy, Wisconsin.

These actions represent progress in properly training finance personnel prior to deployment to Iraq and Kuwait. However, the Army could further improve its training by integrating the Army and DFAS training programs for finance personnel. In addition, the Army should ensure that finance soldiers from the Active, Reserve, and National Guard components all receive the same training prior to deployment to Iraq or Kuwait.

Clear Accountability in the Payments Process. Responsibilities for controls and accountability for commercial payments made at Army contingency disbursing stations are not adequately defined. DFAS Rome has documented its procedures for processing electronic transaction data and original payment support documentation received from Army contingency disbursing stations in Iraq and Kuwait. However, Army and DFAS roles and responsibilities related to controls and accountability for the contingency commercial payment process have not been formalized.

To improve commercial payment processing and related controls, the Army and DFAS agreed that DFAS Rome would become responsible for certifying and making non-cash commercial payments previously made in Kuwait. This transfer of responsibility was completed in September 2007. To support this task, DFAS deployed vendor pay and military pay subject matter experts to Iraq and Kuwait.

The contingency disbursing stations in Kuwait will continue to validate the contract, invoice, and receiving report documents for each payment, but they will send these documents to DFAS Rome using the Electronic Data Management system. DFAS Rome will calculate and certify each payment and create a disbursement file to be sent to the Disbursing Operations Directorate at DFAS Indianapolis Operations for payment.

To ensure clear accountability for each organization, the Army and DFAS should use a memorandum of agreement to define the specific roles and responsibilities of each organization in this new commercial payment process. This memorandum of agreement should also document any other Army and DFAS informal agreements on roles and responsibilities related to new commercial payment processes discussed or recommended in this report. Specifically, the memorandum of agreement should document Army and DFAS roles and responsibilities for the following actions related to commercial payment vouchers:

- submission and retention,
- scanning,
- pre-submission and post-submission reviews,
- follow-up on incomplete vouchers,
- use of management performance indicators,
- training, and
- establishing a process for identifying payments that may be candidates for a loss-of-funds investigation or a recovery audit.

These process changes will improve future oversight and accountability for commercial payments. Establishing a process to identify questionable or improper payments will help ensure that loss-of-funds investigations and recovery audits are performed to recover funds.

Importance of Internal Controls

Internal control systems provide reasonable assurance that programs are operating as intended and are achieving expected outcomes. Internal controls should also ensure that there is sufficient evidence that goods and services were properly procured and received. The Army's weak internal controls over commercial payments in Iraq and Kuwait did not permit reasonable assurance that Army contingency disbursing stations properly authorized commercial payments and maintained the supporting documentation. In addition, the lack of internal controls resulted in either no audit trail or in a complex audit trail, which hindered the search for supporting documents. Effective internal controls serve to safeguard assets and help to prevent and detect errors and fraud. Ineffective internal controls can result in missing or inadequate commercial payment documentation. In addition, ineffective internal controls can result in inadequate audit trails and unreliable accounts payable and expense amounts reported on Army and DoD financial statements. Ineffective internal controls could create an environment conducive to fraudulent activity or improper use of funds. We referred 28 vouchers totaling \$35.1 million to the Defense Criminal Investigative Service (DCIS) for potential follow-up because of their support deficiencies the unusual nature of the transaction; or because they pertained to payees of interest to DCIS.

As a result of internal control deficiencies over commercial payments, we were unable to determine whether all of the payments reviewed were disbursed as intended. The USD(C)/CFO and DFAS need to be directly involved in supporting military finance operations to ensure DoD funds are used properly in support of our troops in the Global War on Terror.

Annual Assurance Statement

The FY 2007 Army Annual Statement of Assurance did not identify the lack of commercial payment documentation as a material internal control weakness. Because of the magnitude of the commercial payment documentation deficiencies and the related vulnerability to fraud, waste, and abuse, the Army should address the identified internal control deficiencies in its Annual Statement of Assurance as material weaknesses.

Management Comments on the Finding and Audit Response

Under Secretary of Defense (Comptroller)/Chief Financial Officer Comments. The USD(C)/CFO provided additional comments on the report on May 15, 2008. She stated that:

The auditors correctly report that the Department did not provide comprehensive guidance for preparing and retaining payment documentation during contingency operations, a shortcoming we have since remedied. The audit identified areas where management controls needed improvement, but did not acknowledge the improvements made to address these areas. For instance, we changed documentation policies to require the retention of contracts, invoices, receiving reports, and payment vouchers with the accounting office (Rome, New York) to enhance the audit trail for contingency operation payments. We implemented a monthly balanced scorecard review to ensure compliance with this revised policy. Another significant control is complete fielding of the Deployable Disbursing System to all in-theater payment activities. Finally, many payments previously entitled and paid in theater are now processed by the Rome, New York DFAS site.

In addition, the DFAS is implementing a phased strategy to transfer all electronic fund transfer (EFT) payments from Iraq and Afghanistan to DFAS Rome, NY. Currently, DFAS Rome makes EFT payments that exceed \$250,000 and by October 2008, will make all EFT payments for Iraq and Afghanistan. Finally, the DFAS is implementing a document imaging process in theater to ensure all payment documentation is transmitted to DFAS Rome for retention. The DFAS has also provided training in disbursing, vendor pay and accounting operations for deployed and deploying units. A forward deployed cell of DFAS personnel was established in-theater to relieve warfighters of the administrative functions associated with documentation processing and to provide other assistance, as needed.

Audit Response. We had previously recognized most of the DoD actions in the finding; however, we incorporated the USD(C)/CFO additional comments above to ensure that management actions are adequately disclosed. In addition, we are currently performing an audit of the Deployable Disbursing System to determine if the internal controls are adequate and the data processed is reliable.

Deputy Chief Financial Officer Comments. The Deputy Chief Financial Officer provided comments to the finding. The Deputy did not agree with the methodology used to estimate the projected dollar amount of payments lacking information or supporting documentation. The Deputy added the estimated dollar amounts do not distinguish between “critical” and “noncritical” errors.

Audit Response. We projected the results of the sample using a stratified sampling design that yielded unbiased, but conservative estimates. Appendix B provides details regarding our sampling plan and results. We added clarifying language to better distinguish between essential information needed to support a proper payment and other information that was not essential to determining entitlement. We estimated that the Army made \$1.4 billion in commercial payments that lacked the minimum documentation and information for payment. Another estimated \$6.3 billion in commercial payments did not comply with other statutory and regulatory requirements, but did contain supporting information essential to support a proper payment

Army Comments. The Deputy Assistant Secretary of the Army (Financial Operations) provided comments to the finding. The Deputy Assistant Secretary stated that the report was inconsistent with DoD policy that the report cited the lack of compliance with the PPA while indicating the PPA does not apply. The

Deputy Assistant Secretary stated, “It is recognized that there were administrative errors, the audit trail is difficult to follow, and a small percentage of vouchers require follow-up due to critical deficiencies such as a missing payee signature.” Further, the Deputy Assistant Secretary stated, “If the auditors had been able to travel to the theater to follow the appropriate audit trails or to Fort McCoy to observe the training being given to deploying units, the audit report would be more informative and identify specific areas of concern.”

Audit Response. The DFAS accounting policy office disclosed the inconsistency between DoD policy and the PPA on November 29, 2007. We have made recommendations to USD/AT&L and USD(C)/CFO to resolve the inconsistency and the applicability of PPA to military contingency operations.

Resolving an inconsistency and the applicability of PPA to military contingency operations does not preclude ensuring that essential information is obtained to support a proper payment. Additionally, we do not believe the lack of adequate documentation and information supporting commercial payments is an administrative error. A minimum level of information, such as an invoice and a receiving report, is essential to determine whether an entitlement exists for a payment. As discussed in the finding, the Army disbursements of an estimated \$1.4 billion lacked essential information supporting proper payment.

We agree with the Deputy Assistant Secretary’s comments that indicate the difficulty of an audit trail in a military contingency operation. However, our concern is more than an adequate audit trail. Rather, we are concerned that there are significant gaps in internal controls over commercial payments made in a military contingency operation. Those gaps in internal controls could create situations where we are more vulnerable to fraud, waste, and abuse. Certifying officials should have sufficient information to determine whether an entitlement is proper for payment. For example, signatures from certifying officials, receiving officials, and payees are essential internal controls to authenticate entitlement and approval of contractor and vendor invoices for payment. In addition, documentation needed to support many of the sampled commercial payments was not readily available at the assigned accounting office as required by DoD FMR, volume 10, chapter 8. DoD IG auditors deployed to Iraq attempted to locate missing voucher documentation but were generally unsuccessful. In addition, the Assistant Inspector General, Defense Financial Auditing Service, granted the Army and DFAS an additional 90 days to locate missing documentation for 152 payment vouchers after we had completed our initial audit work. As discussed in the finding, the Army and DFAS did not locate the missing documentation and information for 125 of 152 payment vouchers.

We held discussions with responsible Army personnel at the Soldier Support Institute, Fort McCoy, and the Army Finance Command and obtained the curricula and other information on financial training. Based on documentation obtained and discussions held, we determined that the training program needed improvement. As discussed in the finding, we also discussed training with Army finance personnel actually deployed in Iraq. As a result of this audit, the USD(C)/CFO, the Army, and DFAS have taken several actions to improve internal controls over making commercial payments and the training of finance personnel.

Additional Management Comments. On May 13, 2008, we met with representatives from USD (C)/CFO, Army, and DFAS to discuss this report. During this meeting, the Deputy Comptroller asked us to consider additional verbal comments regarding the results of our audit work. The Principal Deputy Under Secretary of Defense (Comptroller) stated that the Army and DFAS disagreed with our conclusion that 125 commercial payments were not properly supported and with our statistical projection that a total of \$1.4 billion in commercial payments lacked minimum supporting documentation. He stated that the Army had done a review of these 125 disbursements and, based on additional information that they obtained, they concluded that these were all valid payments and 123 of these disbursements had the appropriate supporting documents.

The Army provided a memorandum dated May 15, 2008, that reconfirmed their position made at the May 13, 2008, meeting. The Army stated that:

As directed by your recommendation, we expanded the review of the 125 payments to include documentation maintained by theater contract, entitlement, and payment activities to determine if the payments were properly supported. Our review applied the legal certification criteria and supporting information requirements identified in the Comptroller's memorandum of September 14, 2007. That memorandum set forth the Department's legal requirement for commercial payment certification in contingency operations.

We matched payment, invoice, and receiving report for 96 percent of the 702 payments, and conclude that twelve payment invoices could constitute loss of funds. We were able to validate ten of these payments, and continue to research the remaining two payments made by a disbursing station that closed in December 2004.

Based on these findings, the audit's conclusion that "the Army made an estimated \$1.4 billion in commercial payments that lacked minimum supporting documentation" should be modified. Our expanded review of in-theater documentation indicates all payments were properly documented. The audit's estimates should be adjusted accordingly.

Audit Response. During the May 13, 2008, meeting, the Army and DFAS representatives did not provide additional supporting documentation to us and therefore, we could not validate their assertion that these payments were valid or supported by appropriate documentation. In addition, we are unsure what criteria were used to determine whether these disbursements were valid and properly supported. In addition, the Army and DFAS representatives did not explain how additional documentation was obtained when the auditors found that some payments had documents, like a receiving report or invoice, but lacked essential information such as the identification of goods or services received or a proper approval.

The Army and DFAS were provided many opportunities to produce the missing payment information. On May 3, 2007, we provided the Army and DFAS a list of vouchers in our audit sample. On May 21, 2007, we provided the Army an additional 90 days to find the missing documentation for the 152 vouchers considered to be unsupported payments. On July 23, 2007, we met with DFAS personnel to review additional supporting documentation found by DFAS and the Army. Because of this meeting, we reduced the number of unsupported vouchers

to 125. On November 16, 2007, and January 15, 2008, we issued discussion draft reports. In addition, neither DFAS nor Army stated that they found additional documentation in their comments provided to the draft report of February 11, 2008.

Because the Army has not provided the information required to validate their assertion, we did not modify the report. The Army certifying officials approved 702 payments based on the documentation attached to the vouchers at the time of the payment rather than the assertions the Army made in its May 15, 2008, memorandum. In addition, much of the required information was not recorded on the invoices and receiving reports. Section 3325, title 31, U.S.C. require that the certifying officials are responsible for the information on the voucher and supporting records.

Recommendations, Management Comments, and Audit Response

A.1. We recommend that the Under Secretary of Defense for Acquisition, Technology, and Logistics and the Under Secretary of Defense (Comptroller)/Chief Financial Officer coordinate with the Office of Management and Budget to resolve conflicting guidance in 5 Code of Federal Regulations Part 1315 (2001) regarding the documentation requirements for disbursements made in military contingency operations.

Management Comments. The Director, Defense Procurement, Acquisition Policy, and Strategic Sourcing and the Deputy Chief Financial Officer concurred and stated that they are engaged with OMB in resolving the issue. The Deputy is waiting for OMB to provide an expected response date.

Audit Response. The Director, Defense Procurement, Acquisition Policy, and Strategic Sourcing and the Deputy Chief Financial Officer comments are responsive to the recommendation.

A.2. We recommend that the Under Secretary of Defense (Comptroller)/Chief Financial Officer update the DoD 7000.14-R, “DoD Financial Management Regulation” with the following changes:

a. Consolidated guidance that identifies the Federal Acquisition Regulation and DoD 7000.14-R, DoD Financial Management Regulation requirements to support commercial payments and address the deficiencies that are listed in Appendix E.

Management Comments. The Deputy Chief Financial Officer partially concurred and stated that they will update the DoD FMR to clarify financial management policy, as necessary, contingent upon the resolution of the applicability of the PPA to contingency operations. The Deputy is waiting for OMB to provide an expected response date.

Audit Response. The recommendation addressed the consolidation of commercial payment support requirements within the DoD FMR because it

provides requirements for use in day-to-day financial operations, and commercial payment support requirements should be readily accessible to finance personnel. Consolidated guidance would help users more readily identify essential information needed to support proper payments. The recommendation further addressed the criteria needed to support a payment, as shown in Appendix E. Resolving the applicability of the PPA to contingency operations does not preclude incorporating the September 14, 2007, USD(C)/CFO policy memorandum, "Certified Commercial Payments in Contingency Operations," into the DoD FMR. On May 16, 2008, the office of the USD(C)/CFO notified us that it had incorporated the policy memorandum into the DoD FMR. We request that the Deputy provide additional comments to the final report on the consolidation of commercial payment support requirements.

b. Clearly identify the appropriate uses and payment thresholds for the SF-44, as addressed in the Federal Acquisition Regulation and the Defense Federal Acquisition Regulation Supplement.

Management Comments. The Deputy Chief Financial Officer partially concurred and suggested that the recommendations be redirected to USD/AT&L, saying that identifying the appropriate uses and payment thresholds for the SF-44 are under the purview of the USD/AT&L. He agreed to update the DoD FMR, as necessary, to reflect any SF-44 policy changes by USD/AT&L.

Audit Response. The DoD FMR is incomplete in its definition of the appropriate use or payment thresholds of the SF-44, and the guidance is scattered throughout the FAR and DFARS. Therefore, the USD(C)/CFO should update the DoD FMR on its definition of the appropriate use and payment thresholds of the SF-44 and ensure consistency with the FAR and DFARS. We request that the Deputy reconsider his position and provide comments to the final report.

A.3. We recommend that the Assistant Secretary of the Army (Financial Management and Comptroller):

a. Review the 125 commercial payments that were not properly supported and, if the errors cannot be resolved, determine whether a loss of funds investigation or other investigative action, such as a payment recovery audit, is required to ensure that the payment was not improper.

Management Comments. The Deputy Assistant Secretary of the Army (Financial Operations) partially concurred and stated that the Army has initiated review of commercial payments that were not properly supported. The Army will initiate a formal loss of funds investigation if a reasonable assurance of payment cannot be ascertained.

Audit Response. The Deputy Assistant Secretary of the Army (Financial Operations) did not specify whether he would review the 125 commercial payments that we determined were not properly supported. We request that the Deputy Assistant Secretary provide additional comments to the report to clarify his response to our recommendation.

b. Require that certifying officers at all Army finance offices complete a standard checklist of required commercial payment support elements developed from the Federal Acquisition Regulation and the DoD 7000.14-R, DoD Financial Management Regulation, before a payment voucher is forwarded to its appropriate disbursing and accounting office.

Management Comments. The Deputy Assistant Secretary of the Army (Financial Operations) partially concurred with the recommendation. The Deputy Assistant Secretary stated that the Army will revise the current checklist as necessary to address PPA and employer identification number requirements. He added that the Army would direct deployed Army finance offices to use the checklist.

Audit Response. The Deputy Assistant Secretary of the Army (Financial Operations) comments did not address whether he would use the FAR or the DoD 7000.14-R to derive a standard checklist. We request that the Deputy Assistant Secretary provide additional comments to the final report.

c. Develop an integrated training approach providing adequate and timely training in disbursing, vendor pay, and accounting operations to finance personnel deployed to contingency disbursing stations.

Management Comments. The Assistant Secretary of the Army (Financial Operations) partially concurred and stated that the Army has an integrated disbursing and vendor pay training program for units deploying to theater, and it is under continual review and improvement.

Audit Response. The Army response does not indicate specific actions taken to improve its integrated and vendor pay training program for units deployed to theater. We request that the Deputy Assistant Secretary provide additional comments describing actions taken to improve its integrated and vendor pay training program for units deployed to theater.

d. Address the internal control deficiencies identified in this report in the Army Annual Statement of Assurance as material weaknesses.

Management Comments. The Assistant Secretary of the Army (Financial Operations) partially concurred and stated that complex audit trails related to vendor payments made in a contingency theater of operations will be identified as a material weakness in the Army's next Annual Statement of Assurance.

Audit Response. The Army should update its Annual Statement of Assurance to identify the following internal control deficiencies as material weaknesses related to military contingency operations: availability of supporting documentation, payment voucher quality, training of Army finance personnel, and clarification of Army and DFAS responsibilities in the commercial payment process. We request that the Deputy provide additional comments to the final report that address the specific internal control weaknesses identified above.

A.4. We recommend that the Assistant Secretary of the Army (Financial Management and Comptroller) and the Director, Defense Finance and Accounting Service establish a formal agreement that clarifies each organization's distinct responsibilities to ensure proper accountability for commercial payment vouchers.

Management Comments. The Deputy Assistant Secretary of the Army (Financial Operations) and the Deputy Director, DFAS Standards and Compliance concurred with the recommendation. The Deputy Assistant Secretary stated that the Army would work with DFAS to update the existing standard operating procedures and formalize it in a memorandum of agreement. The Deputy Director stated that memoranda of agreement were executed for DFAS Rome becoming responsible for certifying and making non-cash commercial payments previously made by Kuwait, Qatar, and U.S. Army Central Command Support Teams. The Deputy Director also stated that DFAS will continue working with the Army to establish agreements clarifying each organization's responsibilities.

Audit Response. The Deputy Assistant Secretary of the Army (Financial Operations) and Deputy Director, DFAS Standards and Compliance, actions are responsive to the recommendation.

B. Contingency Operations and the Prompt Payment Act

The DoD 7000.14-R, DoD Financial Management Regulation and Defense Federal Acquisition Regulation Supplement did not contain guidance addressing procedures to be used in a military contingency environment. The Office of Management and Budget allowed the DoD discretion in establishing the scope of contingency operations in 5 Code of Federal Regulations 1315 when applying the Prompt Payment Act. However, DoD has not established procedures addressing contingency operations. In addition, DoD needs to obtain clarification on the intent of the Office of Management and Budget regulation. As a result, DoD personnel relied upon the requirements of the DoD 7000.14-R, DoD Financial Management Regulation and Defense Federal Acquisition Regulation Supplement for making and processing commercial payments in Iraq and Kuwait.

Prompt Payment Act Exception

The OMB has implemented the PPA, as stated in 5 Code of Federal Regulations (C.F.R.) Part 1315 (2001). 5 C.F.R. Part 1315, section 1315.1 states that vendor payments related to military contingency operations are exempt from the PPA. According to the DoD Office of General Counsel, DoD had discretionary authority to implement PPA in a contingency operation. The Under Secretary of Defense for Acquisition, Technology, and Logistics (USD[AT&L]) and the USD(C)/CFO did not promulgate guidance implementing the PPA exception. Before DoD can develop guidance, it must obtain clarification from OMB on defining contingency operations and when the C.F.R. provision applies to making payments.

DoD Guidance. The USD(AT&L) and the USD(C)/CFO are responsible for implementing policies in the FAR, DFARS, or DoD FMR that are consistent with, and meet the intent of, statutory and regulatory requirements that are applicable to DoD. The FAR, DFARS, and DoD policy do not address contingent operations.

The Federal Acquisition Regulation and the Defense Federal Acquisition Regulation Supplement. The USD(AT&L), through the office of Defense Procurement and Acquisition Policy, is responsible for all acquisition and procurement policy matters in the DoD. The Defense Procurement and Acquisition Policy office serves as an adviser to the USD(AT&L) on acquisition and procurement strategies for DoD acquisitions and assists in maintaining the FAR and the DFARS. Neither the FAR nor the DFARS provides policy on proper contracting requirements specific to military contingency operations. Because of the absence of an established policy, the contracts we reviewed continued to include and execute PPA provisions.

DoD 7000.14-R, DoD Financial Management Regulation. The USD(C)/CFO provides all DoD components with the policies, regulations, and procedures for DoD financial management regulation through the DoD FMR. It governs financial management by establishing and enforcing requirements, principles, standards, systems, procedures, and practices necessary to comply

with statutory and regulatory requirements applicable to DoD. Compliance with the DoD FMR is mandatory for all DoD Components, and all revisions to the regulation are the responsibility of the USD(C)/CFO. The DoD FMR does not address the PPA exception for military contingency operations. In the absence of policy addressing military contingency operations, the Army utilized existing DoD FMR provisions to pay vendors and contractors.

DoD should develop policy on contingent operations and coordinate the policy with OMB. The DoD policy on contingency operations should include:

- a definition of when contingency operations will activate the exception from the PPA,
- identification of the geographic region or contracts to which the exception would apply, and
- procedures to be used as an alternative to the PPA that would describe the contract clauses required to ensure that commercial payments are made appropriately.

Code of Federal Regulations. DoD needs to coordinate with the OMB to obtain clarification of the intent of the PPA exception for military contingency operations and to clarify ambiguities in 5 C.F.R. Part 1315 (2001). The C.F.R. was unclear regarding the scope of a contingency military operation as it related to application of the PPA. One USD(AT&L) official stated that contingency operations end 30 days after deployment. 5 C.F.R. Part 1315, which implements the PPA, has conflicting guidance related to payments made in military contingency operations. 5 C.F.R. Part 1315, section 1315.5 states that for emergency payments, including payments made under a military contingency, “Vendors shall be entitled to interest penalties if invoice payments are made after the payment due date.” However, Section 1315.5 conflicted with 5 C.F.R. Part 1315, section 1315.1. The Army disbursing stations had to rely upon the DFARS and DoD FMR guidance in processing contract and vendor payments in Iraq and Kuwait. In our sample of 702 commercial payment vouchers, the Army made 46 payments with interest penalties of \$275,887.

Management Actions

As a result of the draft report, USD (AT&L) requested an opinion from the DoD Office of General Counsel. The General Counsel issued a legal opinion on March 4, 2008, recognizing the “obvious incongruity” within 5 C.F.R. Part 1315 (2001). The General Counsel also stated that:

In the face of this regulatory inconsistency, the Department has sufficient legal authority to pay interest penalties pending resolution of the regulatory problem...it is not improper for the Department to avail itself of the benefits of the Act (early payment discounts), nor to accept the burden of the Act (paying interest on late payments.)”

As a result of this legal opinion, we revised this finding. We have removed the statements that the Army inappropriately applied the PPA to commercial

payments made for military contingency operations that resulted in potential improper payments. We also clarified our position on the need for DoD to develop a policy that addresses the 5 Code of Federal Regulations 1315 exemption.

Recommendations, Management Comments, and Audit Response

Revised, Deleted, and Renumbered Recommendations. We have revised Recommendation B.1.a. and deleted Recommendation B.1.b. addressed to the USD/AT&L and the USD(C)/CFO. We revised Recommendation B.1.a. to remove the wording to discontinue making interest payments. We also deleted Recommendation B.1.b. to take appropriate actions to resolve whether previous interest payments taken under the PPA for military contingency operations were justified or whether other actions are required to resolve the payments made. We revised and deleted these recommendations because the DoD Office of General Counsel issued a legal opinion on March 4, 2008 that stated the Department has sufficient legal authority to pay interest penalties. Recommendation B.1.a. was renumbered to B.1.

B.1. We recommend that the Under Secretary of Defense for Acquisition, Technology and Logistics and the Under Secretary of Defense (Comptroller)/Chief Financial Officer coordinate to obtain legal advice to determine the impact of contract clauses that require making interest payments for existing contracts in military contingency operations.

Management Comments. The Director, Defense Procurement, Acquisition Policy, and Strategic Sourcing and the Deputy Chief Financial Officer concurred with the recommendation. They stated that the Department's Office of General Counsel concluded that the Department has legal authority to pay interest penalties and retain early payment discounts. The Deputy added that as a result, the Department will continue to pay the interest payments and take discounts in accordance with the terms and conditions of the existing contracts. However, the Deputy is engaged with both OMB and USD/AT&L in resolving the inconsistency in OMB's regulation regarding the applicability of the PPA to contingency operations.

Audit Response. The Director, Defense Procurement, Acquisition Policy, and Strategic Sourcing and the Deputy Chief Financial Officer comments are responsive.

B.2. We recommend that the Under Secretary of Defense for Acquisition, Technology and Logistics update the Federal Acquisition Regulation and the Defense Federal Acquisition Regulation Supplement to provide guidance that addresses the Office of Management and Budget's exception to the Prompt Payment Act for payments related to military contingency operations. The guidance should specify the processes and contract clauses to be used in cases where exceptions to the Prompt Payment Act apply.

Management Comments. The Director, Defense Procurement, Acquisition Policy, and Strategic Sourcing concurred with the recommendation and stated that they will update the Federal Acquisition Regulation and the Defense Federal Acquisition Regulation Supplement to be consistent with OMB after it resolves the inconsistencies in its own regulations.

Audit Response. The Director's comments are responsive.

B.3. We recommend that the Under Secretary of Defense (Comptroller)/Chief Financial Officer update the DoD 7000.14-R, "DoD Financial Management Regulation," to provide guidance that addresses the Office of Management and Budget's exception to the Prompt Payment Act for payments related to military contingency operations. The guidance should specify the processes to be used in cases where exceptions to the Prompt Payment Act apply.

Management Comments. The Deputy Chief Financial Officer partially concurred with the recommendation and stated that they are engaged with USD/AT&L and OMB in addressing the inconsistencies in the regulation with respect to the applicability of the PPA to contingency operations. The Deputy added that they will update the DoD FMR as necessary to clarify any related financial management policy with respect to contingency operations.

Audit Response. The Deputy Chief Financial Officer comments are responsive.

C. Payments to Foreign Governments

DoD did not ensure that \$1.8 billion of seized and vested assets payments made to Iraqi representatives were adequately accounted for and auditable, as prescribed by Executive Order 13290. In addition, DoD did not maintain a complete audit trail for \$134.8 million in Commander's Emergency Response Program (CERP) payments made to representatives of foreign governments. DoD did not have policies in place to ensure that:

- finance personnel obtained and maintained documentation supporting the justification and use of seized and vested asset payments; and
- finance personnel properly supported and reconciled the payment of CERP funds to Coalition Partners.

As a result, DoD was unable to provide reasonable assurance that the seized and vested asset funds were accounted for as prescribed and that CERP funds provided to Coalition Partners were used for the purposes intended.

Background

Seized and Vested Assets Payments. When Iraq invaded Kuwait in August 1990, the U.S. froze Iraqi assets held in U.S. banks. On March 20, 2003, the President issued Executive Order 13290, which vested the Iraqi assets in a U.S. Treasury Special Purpose Account established at the Federal Reserve Bank of New York. This U.S. Treasury Special Purpose Account, or vested assets fund, totaled approximately \$1.9 billion.

Seized assets are former Iraqi regime monies confiscated by coalition forces during the invasion of Iraq. Coalition military forces seized \$926.8 million in funds from the former Iraqi regime. A Presidential memorandum dated April 30, 2003, provided DoD the authority to use seized and vested assets to assist the Iraqi people and support the reconstruction of Iraq. The memorandum also directed the DoD to prescribe procedures to ensure that all seized and vested Iraqi assets would be properly accounted for, audited, and used to assist the Iraqi people. DoD prescribed procedures in the USD(C)/CFO memorandum, "Appendices for Procedures Applicable to Vested and Seized Iraqi Property," dated July 31, 2003.

A Deputy Secretary of Defense memorandum dated May 29, 2003, gave control of these funds to the Coalition Provisional Authority (CPA). One of the priorities facing the CPA was to restart the Iraqi economy by paying Iraqi civil servants. To accomplish this, the CPA provided the Iraqi ministries with funds through an Iraqi representative. The CPA provided these funds from the seized and vested asset accounts. The Iraqi representative would sign for the cash provided and was responsible for distributing the funds to individual civil servants.

Coalition Partner Payments. Public Law 108-375, “The Ronald W. Reagan National Defense Authorization Act for FY 2005,” October 28, 2004, authorized DoD military commanders in Iraq to use CERP funds to immediately respond to urgent humanitarian relief and reconstruction requirements within their areas of responsibility by carrying out programs to assist the Iraqi people. DoD prescribed guidance for the use of CERP funds in the USD(C)/CFO memorandum, “Commander’s Emergency Response Program (CERP) Guidance,” dated July 27, 2005. This guidance allowed CERP funds to be used to assist the Iraqi people in several areas:

- for repairs and condolence payments after combat operations;
- for protective measures (such as fencing, barrier materials, and guard towers) to enhance durability and survivability of critical infrastructure sites; and
- to initiate and execute a variety of projects in their areas of responsibility, including construction projects.

Both U.S. Forces and Coalition Partners perform CERP-funded projects. The Coalition Partners comprise three of the six major subordinate commands headquartered throughout Iraq. As of FY 2006, the individual major subordinate commands consisted of:

- Multi-National Division-Baghdad – U.S. Army;
- Multi-National Division-Center South – Poland;
- Multi-National Division-North – U.S. Army;
- Multi-National Division-Northeast – South Korea;
- Multi-National Division-Southeast – United Kingdom; and
- Multi-National Force-West – U.S. Marine Corps.

Payment Vouchers Review

DoD did not ensure that \$1.8 billion of seized and vested assets payments made to Iraqi representatives were adequately accounted for and auditable, as prescribed by Executive Order 13290. In addition, DoD did not maintain a complete audit trail for \$134.8 million in CERP payments made to representatives of foreign governments. The 75 vouchers in our sample were for payments to Iraqi ministries and Coalition Partners, as shown in Table 3. The vouchers for seized and vested assets payments did not have sufficient supporting documentation and audit trails to verify that funds were accounted for as prescribed by Executive Order 13290. The vouchers for CERP payments made to Coalition Partners did not have sufficient supporting documentation and audit trails to verify that funds were used for the purposes intended. Audit trails are necessary to demonstrate the accuracy, completeness, and support of payments. As a result, DoD was unable

to provide reasonable assurance that the seized and vested asset funds, and CERP funds provided to Coalition Partners were used to assist the Iraqi people.

<u>Payment type</u>	<u>Number of Vouchers</u>	<u>Amount (in millions)</u>
Seized and Vested Assets	53	\$ 1,825.8
Coalition Partners	22	\$ 134.8
Totals	75	\$ 1,960.6

Seized and Vested Assets

Fifty-three payment vouchers, totaling \$1,825.8 million, were for seized and vested asset payments to the Iraqi ministries for Iraqi civil servant salaries and ministry operations. However, DoD did not maintain sufficient documentation supporting the justification and use of seized and vested asset payments to Iraqi ministries, nor did it provide adequate guidance to the Iraqi ministries regarding accounting and documentation requirements.

Supporting Documentation. The payment vouchers contained the certifying officer’s appointment letter, a “Purchase Request and Commitment” form, and a brief description of the purpose of the payment, stating whether it was for Iraqi civil servant salaries; pensions; ministry operations; or repair and reconstruction. However, this documentation was inadequate because it did not provide the audit trail needed to validate who actually received the funds or how the funds were to be used. Information omitted from the voucher included the name of the Iraqi ministry to whom the funds were to be provided and a specific accounting of how the funds were to be used (such as the number of Iraqi civil servants to be paid).

For example, our sample included a \$320 million cash payment to an Iraqi representative for Iraqi salary payments. The only supporting documentation in the payment voucher were two “Purchase Request and Commitment” forms to obligate the funds and another document that indicated the amount of funds being requested. These documents did not account for how the funds were used for salaries or the benefit of the Iraqi people. The name of the Iraqi ministry to whom the funds were to be provided and the number of Iraqi civil servants to be paid were omitted from the voucher. This information could have been provided by attaching a spending plan or budget.

We were unable to obtain the spending plans or reconcile vouchers with CPA budgetary information. The payment vouchers we reviewed in our sample did not have spending plans attached, and we were unable to obtain them from the Office of the Under Secretary of Defense (Comptroller) or the Army Headquarters

Budget Office. In addition, the CPA budgetary information did not provide enough detail for an audit trail. The Special Inspector General for Iraq Reconstruction (SIGIR) reported that the “CPA did not maintain adequate documentation to support spending plans, budget disbursements or cash allocations made by coalition forces.”⁵

Seized and Vested Asset Guidance. DoD did not provide adequate guidance to ensure that finance personnel obtained and maintained documentation supporting the justification and use of seized and vested asset payments. DoD did not provide guidance over seized and vested assets until May 2003, and it did not address roles, responsibilities, and procedures regarding the use of seized and vested assets. DoD provided detailed guidance for seized and vested assets when the USD(C)/CFO issued a memorandum on “Administering, Using and Accounting for Vested and Seized Property,” dated July 31, 2003. However, by July 2003, \$1.2 billion of seized and vested assets had already been disbursed to the Iraqi ministries.

This USD(C)/CFO memorandum provided guidance to the CPA for working with the Iraqi ministries to identify and develop requirements for spending plans. The CPA was to provide the Office of the Under Secretary of Defense (Comptroller) and the Army Headquarters Budget Office with the spending plans. Although these spending plans would have provided support for the accounting and use of seized and vested asset payments, the DoD guidance did not require them to be provided to disbursing personnel making the payments. DoD should develop guidance for documentation needed to support seized and vested asset payments to foreign government representatives. To facilitate transparency, the guidance should require seized and vested asset payment vouchers to be supported with documentation such as the spending plans used in determining the amount of funds to be paid.

Coalition Partners

Twenty-two payment vouchers, totaling \$134.8 million, were for CERP payments to Coalition Partners to initiate and execute a variety of non-construction and construction projects in their areas of responsibility. DoD could not provide a complete audit trail for CERP payments. Specifically, documentation was insufficient, and reconciliations were not performed. DoD guidance did not contain requirements for documentation and reconciliation of CERP payments.

Audit Trail. None of the 22 CERP payment vouchers we reviewed contained sufficient supporting documentation to provide reasonable assurance that these funds were used for their intended purposes. For example, one payment voucher provided to Multi-National Division – Northeast (South Koreans) for \$8 million contained only a “Purchase Request and Commitment” form and a memorandum acknowledging that foreign Coalition forces cannot be certified as paying agents for U.S. Government funds. From this documentation, we could not verify that

⁵ Office of the Special Inspector General for Iraq Reconstruction Audit Report: “Oversight of Funds Provided to Iraqi Ministries through the National Budget Process” (Report No. 05-004), dated January 30, 2005.

the funds provided to Coalition Partners were used for CERP purposes. In addition, the Army had not performed any reconciliation of funds paid to Coalition Partners. The Army relied on the Coalition Partner's comptroller to perform the reconciliation. To document CERP payments, the Army required the submission of project folders when projects were completed, but it did not require the reconciliation of payments.

SIGIR also reported that many project files from Coalition Partners did not contain required supporting documentation.⁶ In addition, SIGIR reported that Multi-National Corps – Iraq was unable to supply 29 percent of the requested project files. Multi-National Corps – Iraq guidance required that the Major Subordinate Commands provide the project files for completed project to Multi-National Corps – Iraq Headquarters. The Coalition Partners should have followed this guidance. The vouchers and attached documentation acknowledged that the Coalition Partners were to maintain a record of receipts and invoices that supported the funds issued on the voucher.

Funds Provided to Coalition Partners. DoD did not provide adequate guidance to ensure that payments of CERP funds to Coalition Partners were properly supported and reconciled. Specifically, DoD guidance did not ensure that disbursing personnel obtained and retained documentation supporting the accounting and use of CERP funds provided to Coalition Partners. In addition, DoD has not developed procedures to reconcile CERP funds paid to Coalition Partners. As a result, the Army had limited oversight over CERP payments made to Coalition Partners and could not provide reasonable assurance that CERP funds were used for their intended purposes.

The USD(C)/CFO establishes and supervises the execution of policies and procedures for the accounting and control of CERP funds. The USD(C)/CFO issued guidance on the use of CERP funds through a memorandum, "Commander's Emergency Response Program (CERP) Guidance," dated July 27, 2005. However, this guidance provided limited instruction on the use of Coalition Partners as custodians of U.S. government funds during contingency operations.

The Multi-National Corps – Iraq created guidance for Coalition Partner Major Subordinate Commands to use CERP funds. The Multi-National Corps – Iraq guidance provided the procedures for funding Coalition Partners using CERP funds. However, it did not provide sufficient procedures for supporting payments and reconciling payments of CERP funds to project documentation provided by Coalition Partner Comptrollers. (Reconciliation of CERP payments can be difficult, because one CERP payment voucher can pertain to numerous projects).

To ensure that DoD properly supports and reconciles payments of CERP funds, the USD(C)/CFO should update the DoD FMR, volume 12, chapter 29 to require the reconciliation of funds that are paid to Coalition Partners. The DoD FMR, volume 12, chapter 29 should also be updated so that it is not limited to

⁶ Office of the Special Inspector General for Iraq Reconstruction Audit Report: "Management of the Commander's Emergency Response Program in Iraq for Fiscal Year 2006" (Report No. SIGIR-07-006), dated April 26, 2007.

contingency operations in Iraq and Afghanistan and can apply to future contingency operations that may require the use of Coalition Partners as paying agents.

DoD FMR Contingency Operations Requirements

The DoD FMR has not been updated to address seized and vested assets, and guidance on the use of CERP funds was not added until April 2005. However, to ensure that guidance will be available for future contingency operations, the USD(C)/CFO is in the process of updating the DoD FMR, volume 12 to include a chapter on “Administering, Using and Accounting for Funds and Property during Contingency Operations.” The chapter will incorporate the July 31, 2003, memorandum on procedures for the accountability for seized and vested assets. The procedures were originally developed for Iraq but will be modified for future contingency operations. The DoD FMR on contingency operations should be updated to reflect lessons learned from Iraq so that disbursing transactions made with other countries’ funds are auditable and transparent.

Recommendations, Management Comments, and Audit Response

C. We recommend that Under Secretary of Defense (Comptroller)/Chief Financial Officer update DoD 7000.14-R, “DoD Financial Management Regulation,” volume 12, chapter 29 to:

1. Specify documentation needed to support seized and vested asset payments to foreign government representatives. At a minimum, the policy should require documentation sufficient to provide an audit trail for such payments. The audit trail documentation should include supporting budget details and spending plans that can be reconciled to payment vouchers.

Management Comments. The Deputy Chief Financial Officer partially concurred with the recommendation. The Deputy stated USD(C)/CFO staff are incorporating the July 31, 2003 memorandum titled, “Appendices for Procedures Applicable to Vested and Seized Iraqi Property” into the DoD FMR and adding a section on records retention and disposition during contingency operations. The Deputy stated that he does not agree that the audit trail documentation should include supporting budget details and spending plans that can be reconciled into payment vouchers, arguing that it is not a disbursing office responsibility.

Audit Response. The Presidential memorandum, dated April 30, 2003, prescribed that all seized and vested Iraqi assets would be properly accounted for, audited, and used to assist the Iraqi people. The payments were to be based on spending plans and budgets, which would document the support for the justification and use of seized and vested assets. Without such support, there is no

audit trail that would be needed to meet the prescribed requirement. We request that the Deputy reconsider his position and provide additional comments to the final report.

2. Require the reconciliation of funds that are paid to Coalition Partners.

Management Comments. The Deputy Chief Financial Officer partially concurred and stated that the DoD FMR requires all funds advanced to Coalition Partners to be reconciled when the Coalition Partners complete the assigned mission and turns in the DD Form 1081, Statement of Agent Officer's Account, as a paying agent.

Audit Response. Only the Multi-National Division-Southeast – United Kingdom is reconciling funds using the process described in management's comments. The other Coalition Partners are being provided funds without reconciling. The reconciliation of funds provided to Coalition Partners should be a requirement and should be documented in DoD FMR volume 12, chapter 29. We request that the Deputy reconsider his position and provide additional comments to the final report.

3. Establish policy on the use of Coalition Partners as paying agents that is suitable for use in future contingency operations with other foreign government representatives.

Management Comments. The Deputy Chief Financial Officer partially concurred with the recommendation. He stated that paying agents must be U.S. citizens, and the DoD FMR, volume 5, chapter 2, provides the duties and responsibilities of paying agents. They will continue to require a waiver for all non-U.S. citizens acting as paying agents.

Audit Response. The waiver requirement for Coalition Partners to be paying agents should be documented in the DoD FMR volume 12, chapter 29 or in volume 5, chapter 2. In addition, the waiver request and approval process should also be documented in the DoD FMR. We request that the Deputy reconsider his position and provide additional comments to the final report.

D. Advanced Iraqi Funds

The U.S. Army Corps of Engineers Finance Center has been unsuccessful in its attempts to resolve the \$5.7 million of advanced Iraqi seized and vested asset funds. The Corps Finance Center did not contact the Office of the Under Secretary of Defense (Comptroller) to obtain direction on the disposition of the funds. As a result, the Corps has not made these funds available to pay for Iraqi debts with the U.S. Government.

Iraqi Funds Availability

In January 2006 and October 2006, the Corps Finance Center placed \$5.7 million in unused seized and vested asset advance funds in a suspense account, where they remained unavailable to use for their intended purposes.⁷ Our sample included 3 vouchers totaling \$21.1 million in seized and vested asset advances to the Corps. The Corps provided documentation to support the disbursement of \$17.3 million of these advances. The remaining \$3.9 million in seized and vested asset advances were not used on contracts. The Corps Finance Center attempted to return the \$3.9 million of unused funds to the CPA by wire transfer. However, the funds were returned to a suspense account and remained there for 21 months, until we identified them in September 2007. In addition, we determined that 4 additional advances, totaling \$1.9 million, were also placed into the suspense account.⁸

Iraqi Funds. In a May 29, 2003 memorandum from the Deputy Secretary of Defense, the CPA was given control of Iraqi seized and vested assets (see Finding C). The CPA made payments to the Corps on behalf of the Iraqi Government. As a result, the CPA issued \$5.7 million in Iraqi assets to the Corps. The purpose of these funds was to assist the Iraqi people in the reconstruction of Iraq.

In addition, the Corps billed the Iraqi Government \$32.5 million for services provided. The Iraqi Government has paid the U.S. Government \$21.8 million, and a \$1.5 million credit was applied to an open bill. As a result, there is still a total of \$9.2 million in debt owed to the U.S. Government by the Iraqi Government.

Wire Transfers. In December 2005, the Corps Finance Center attempted to wire transfer \$5.6 million in unused advance funds to the CPA through the Central Bank of Iraq. The unused advance funds were excess funds not used for services

⁷ The DoD FMR defines “advances” as disbursements of money from the Department of Treasury accounts before performance has been certified by an authorized DoD receiving official and “suspense account” as an expenditure account established to account for receipts (1) held temporarily and later refunded or paid into some other fund of the Government, or (2) held by the Government for others and paid out at the direction of the owner.

⁸ Because of rounding, the unused funds, \$3.9 million and \$1.9 million, do not equal the total vested and seized assets of \$5.7 million. In addition, the difference between the total of the three vouchers, \$21.1 million, and the supported vouchers, \$17.3 million is not equal to the \$3.9 million in unused funds, also because of rounding.

provided by the Corps. The Corps Finance Center transferred the funds to a suspense account, where they would remain until the wire transfer was completed. According to the disbursing officer, the Central Bank of Iraq sent the \$5.6 million back to the Corps Finance Center suspense account because the CPA bank account was invalid as a result of the CPA being dissolved in June 2004. The disbursing officer added that as a result of the Central Bank of Iraq returning these funds, the Corps Finance Center did not attempt to return an additional \$0.1 million (the difference between \$5.6 million and the previously mentioned \$5.7 million). Instead, in October 2006 it placed the funds in a suspense account to await final disposition.

The Corps Finance Center tried to identify the appropriate account holder in its initial attempt to transfer the funds to the Central Bank of Iraq. However, after the funds were returned, it did not take the necessary actions to identify the appropriate account holder. The Joint Area Support Group took over the U.S. Government responsibilities formerly handled by the CPA. The Corps Finance Center should have contacted or sought guidance from the USD(C)/CFO and the Joint Area Support Group to identify a resolution for the funds so that the funds could be put to better use. The \$5.7 million of Iraqi seized and vested asset funds remained in a suspense account until September 2007, when the Corps moved them to advance accounts.

Because the funds remained in a suspense account, the Corps Finance Center did not make the \$5.7 million in seized and vested assets available for other Iraqi projects or to pay for Iraqi debts with the U.S. Government. By leaving the funds in a suspense account and not identifying the appropriate account holder, the Corps Finance Center was unable to make the funds available for assisting the Iraqi people in the reconstruction of Iraq in a timely manner.

Management Actions

We had recommended that the USD(C)/CFO collaborate with the Corps to identify an appropriate resolution of the \$5.7 million in seized and vested assets. On December 12, 2007, the Director of Resource Management for the Chief of Engineers issued a memorandum for the USD(C)/CFO requesting guidance on the disposition of funds received from the CPA by the Corps. Specifically, they requested guidance from the Office of the Under Secretary of Defense (Comptroller) regarding the disposition of residual advanced funds currently held by the Corps and the settlement of \$9.2 million delinquent debt owed by the Government of Iraq. As a result of this action by the Corps, we are not making a recommendation.

Management Comments on the Finding and Audit Response

Army Corps of Engineers Comments. Although not required to comment, the Corps stated that as a result of a \$1.5 million credit being applied to an open bill, the original \$10.7 million debt owed by the Government of Iraq was reduced to \$9.2 million. In addition, the Corps stated that putting the funds in a suspense account was appropriate because the CPA no longer existed. They stated that

OUSD(C)/CFO is preparing a memorandum allowing the Corps to liquidate delinquent accounts receivables from the Government of Iraq with the \$5.7 million in Iraqi seized assets.

Audit Response. The report was adjusted to accurately reflect the reduction in debt owed by the Government of Iraq. In addition, the report now reflects that the Corps could not dispose of the funds in a timely manner because the CPA no longer existed.

Appendix A. Scope and Methodology

We conducted this performance audit from May 2006 through December 2007 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions, based on our audit objectives.

We selected a statistical sample from a universe of 183,486 payments valued at \$10.7 billion. See Appendix B for more information on the statistical sample. The universe included commercial and miscellaneous payment vouchers from seven Army contingency disbursing stations located in Iraq, Kuwait and Egypt. Four disbursing stations were in Iraq (numbers 8550, 5579, 8547, and 8589), two were in Kuwait (8551 and 8748), and one was in Egypt (8788). Our statistical sampling approach resulted in the selection of 789 vouchers valued at a total of \$3.5 billion that dated from April 2001 through June 2006. About 98.8 percent of the dollar value of the vouchers in our sample was paid after January 2003. We analyzed the selected payment vouchers to determine whether internal controls over the payment process and disbursement voucher preparation provided reasonable assurance that the payments were properly supported.

We reviewed the statutes and regulations in Appendix D and determined that there were 53 compliance requirements for a vendor or contract payment. We also coordinated the 53 criteria with DFAS Indianapolis Operations Internal Review and Army Finance Command personnel. Of the 53 compliance criteria, we determined that 27 were the minimum necessary to support a payment and mitigate the risk of making erroneous payment. The criteria addressed elements such as missing or defective invoices, missing or defective receiving reports, and uncertified vouchers. We reviewed the 702 sampled commercial payments for compliance with the 27 criteria. If a payment voucher did not meet one or more of the 27 criteria, the payment was considered not minimally supported. The remaining 26 criteria were not considered essential to determine entitlement for payment while in a military contingency operation but were still required for compliance with statutes and regulations. Payment vouchers with errors only in these 26 criteria were considered supportable but noncompliant. We had initially identified 152 payments as not being minimally supported. The DoD OIG provided the Army and DFAS Rome 90 days to locate the missing support. The Army and DFAS found documentation to support an additional 27 of the 152 payments.

In addition, DoD OIG auditors stationed in Iraq researched questions on specific vendor and contract payments. The DoD OIG auditors interviewed finance personnel about disbursing training received prior to their deployment to Iraq. The DoD OIG auditors also coordinated with Army personnel to locate missing voucher documentation.

We reviewed payment vouchers and supporting documentation for 75 payments made to foreign government representatives and compared them with guidance

created as a result of Executive Order 13290 as discussed in Finding C. We reviewed the guidance provided by the Under Secretary of Defense (Comptroller)/Chief Financial Office and the Multi-National Corps – Iraq. We also reviewed payment vouchers to determine whether the supporting documentation provided assurance that funds were used for their intended purposes. We requested spending plans that would support payments from Office of the Under Secretary of Defense (Comptroller)/Chief Financial Office, Army Budget Office, and DFAS. We also obtained budgetary information from the Coalition Provision Authority Web site. We followed up on procedural issues with the Under Secretary of Defense (Comptroller)/Chief Financial Office, and the Multi-National Corps-Iraq to obtain spending plan and budget information.

We reviewed audit reports issued by the Special Inspector General for Iraqi Reconstruction (SIGIR) (see Appendix C.) We also discussed audit results with SIGIR and former SIGIR personnel knowledgeable with the audit work.

We interviewed personnel and reviewed documentation from the Corps Finance Center and the finance and accounting officer from the Gulf Region Division to resolve questions regarding contracts for sewer repairs in Baghdad, Iraq. We also interviewed representatives of the 3rd Army Headquarters to discuss the obligation of funds used Iraq and Kuwait. We decided to defer the review of funding obligations to a follow-on audit.

Use of Computer-Processed Data. We used the Army’s Data Element Management Accounting Report system to select our sample of commercial payments. We tested the reliability of the Data Element Management Accounting Report data during our sampling process, and the data matched the vouchers we reviewed. We did not test the Data Element Management Accounting Report system for completeness. Not evaluating the completeness did not affect the results of the audit.

Use of Technical Assistance. Operations Research Analysts from the Quantitative Methods Directorate used sampling methods to provide the auditors with a statistical sample of vouchers from the universe of vouchers paid by the seven Army contingency disbursing stations. They also projected the not-properly-supported, noncompliant, total-error, and no-error results by voucher and dollar value from the statistical sample over the universe of commercial voucher payments. See Appendix B for details regarding the statistical sample and analysis furnished by the Quantitative Methods Directorate.

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

Appendix B. Statistical Sampling Methodology

Sampling Plan

Sampling Purpose. We used statistical sampling to evaluate the statutory and regulatory compliance of commercial payments made by Army contingency disbursing stations. A statistical sample would allow for the projection of the sample results over the entire population.

Universe. DFAS Indianapolis Operations provided a data file for each of the seven Army contingency disbursing stations containing all commercial payments made from their inception through June 2006. Taken together, the files contained 183,486 records with a total dollar value of \$10,723,982,947.

Sampling Design. We used a stratified sampling design developed by operations research analysts in the Quantitative Methods Directorate of the DoD Office of the Inspector General. The stratified sample provided both large- and small-dollar vouchers but still allowed for the results of the sample to be projected over the entire population. See Table B-1 for the strata breakdown and number of sample items by stratum.

Voucher Value ⁹	Total Value	Size	Sample Size
\$0 < Value ≤ \$25,000	\$ 820,458,198	142,447	50
\$25,000 < Value ≤ \$100,000	1,385,603,726	27,462	150
\$100,000 < Value ≤ \$500,000	2,240,884,590	11,041	150
\$500,000 < Value ≤ \$1,000,000	888,594,888	1,263	100
\$1,000,000 < Value ≤ \$5,000,000	2,351,180,783	1,084	150
Value > \$5,000,000	3,037,260,762	189	189
Total	\$10,723,982,947	183,486	789

Sampling Results

The audit team provided the Quantitative Methods Directorate with sample results for 789 vouchers. The team identified 87 miscellaneous vouchers that were not commercial payments. Table B-2 summarizes the details in each stratum.

⁹ The notation $a < b$ means that a is less than b . The notation $a \leq b$ means that a is less than or equal to b . The notation $a > b$ means that a is greater than b .

Table B-2. Sample Results By Stratum							
Voucher Value	Population Size	Sample Size	Non-commercial Vouchers	Not Properly Supported Errors	Non-compliant Errors	Total Errors	No Errors
\$0 < Value ≤ \$25K	142,447	50	6	19	21	40	4
\$25K < Value ≤ \$100K	27,462	150	5	34	94	128	17
\$100K < Value ≤ \$500K	11,041	150	4	29	102	131	15
\$500K < Value ≤ \$1M	1,263	100	4	15	77	92	4
\$1M < Value ≤ \$5M	1,084	150	12	19	119	138	0
> \$5M	189	189	56	9	124	133	0
Total	183,486	789	87	125	537	662	40

Analysis and Interpretation. The planned analysis included making estimates of each category of errors for vouchers, the dollar values of errors associated with each category of errors, and the summary estimates for total errors. We projected the results of the sample using the original stratified sampling design. This yielded unbiased, but conservative estimates, because the estimated error rates are based on an overstated sample size.

The results for these projections have been calculated at the 90-percent confidence level and are reported below¹⁰:

¹⁰ The formulas we used are based on those in Sampling Techniques, 3rd edition, by William G. Cochran, pp.56-58, 91-95, 107-108.

Table B-3. Not-Properly-Supported Errors			
	Lower Bound ¹¹	Point Estimate ¹²	Upper Bound
Rate	0.241	0.342	0.444
Number	44,148	62,825	81,502

Table B-3 can be interpreted as follows: based on the sample results, we project with 90 percent confidence level¹³ that between 24.1 percent and 44.4 percent of the 183,486 vouchers will have errors that result in not-properly-supported payments, with the point estimate of 34.2 percent. The corresponding number of vouchers ranges from 44,148 through 81,502, with a point estimate of 62,825. Tables B-4, B-5 and B-6 should be interpreted in a similar manner.

Table B-4. Noncompliance Errors			
	Lower Bound	Point Estimate	Upper Bound
Rate	0.368	0.471	0.575
Number	67,525	86,502	105,478

Table B-5 projects the vouchers that will have either a not-properly-supported error or a noncompliance error. The point estimate is 81.4 percent.

Table B-5. Total Errors			
	Lower Bound	Point Estimate	Upper Bound
Rate	0.728	0.814	0.900
Number	133,518	149,327	165,135

Table B-6 projects the vouchers that will be properly supported and have no compliance errors. The point estimate is 8.5 percent.

¹¹ Confidence intervals (called the lower bound and upper bound) are an estimate of a population parameter that consists of a range of values bounded by what are known as the upper and lower confidence limits.

¹² A point estimate is a statistically based estimate within a population boundary that is a single numerical value.

¹³ The confidence level is a number, stated as a percentage, that expresses the degree of certainty associated with an interval estimate of a population parameter.

Table B-6. No Errors			
	Lower Bound	Point Estimate	Upper Bound
Rate	0.023	0.085	0.148
Number	4,152	15,663	27,173

The results for the dollar value projections have been calculated at the 90 percent confidence level and are reported below:

Table B-7. Noncompliance Errors		
Lower Bound	Point Estimate	Upper Bound
\$6,007,917,952	\$6,343,468,645	\$6,679,019,338

Table B-7 can be interpreted as follows: based on the sample results, we project with 90 percent confidence level that the noncompliance error value is between \$6,007,917,952 and \$6,679,019,338, with the point estimate of \$6,343,468,645. Tables B-8, B-9 and B-10 should be interpreted in a similar manner.

Table B-8. Not-Properly-Supported Errors		
Lower Bound	Point Estimate	Upper Bound
\$1,186,987,280	\$1,416,604,003	\$1,646,220,726

Table B-9 projects the error value of the not-properly-supported or noncompliance errors.

Table B-9. Total Errors		
Lower Bound	Point Estimate	Upper Bound
\$7,438,306,313	\$7,760,072,648	\$8,081,838,983

Table B-10 projects the value that will be properly supported and have no compliance errors.

Table B-10. No Errors		
Lower Bound	Point Estimate	Upper Bound
\$328,510,139	\$454,103,727	\$579,697,315

Appendix C. Prior Coverage

During the last five years, the DoD IG, the Army Audit Agency (AAA), the Air Force Audit Agency (AFAA), the Coalition Provisional Authority Inspector General (CPA-IG) and the Special Inspector General for Iraq Reconstruction (SIGIR) have issued ten reports related to out-of-country payments. Unrestricted DoD IG reports can be accessed at www.dodig.mil/audit/reports. Unrestricted AAA reports can be accessed over the Internet at www.aaa.army.mil/reports.htm. Unrestricted CPA-IG and SIGIR reports can be accessed at www.sigir.mil/reports/audit.aspx. Unrestricted AFAA reports can be accessed at www.afaa.hq.af.mil/afck/plansreports/reports.shtml.

DoD IG

DoD IG Report No. D-2008-026, “Management of the Iraq Security Forces Fund in Southwest Asia-Phase III,” November 30, 2007

AAA

AAA Report No. A-2005-0206-FFG, “Validation of the Statement of Accountability, Attestation of Disbursing Station Symbol Number 8551,” June 29, 2005

CPA-IG

CPA-IG Report No. 05-001, “Coalition Provisional Authority Control of Appropriated Funds,” October 22, 2004

CPA-IG Report No. 04-009, “Coalition Provisional Authority Comptroller Cash Management Controls Over the Development Fund for Iraq,” July 28, 2004

SIGIR

SIGIR Report No. 07-006, “Management of the Commander’s Emergency Response Program in Iraq for Fiscal Year 2006,” April 26, 2007

SIGIR Lessons Learned, “Lessons in Contracting and Procurement,” July 2006

SIGIR Report No. 06-002, “Prompt Payment Act: Analysis of Expenditures Made from the Iraq Relief and Reconstruction Fund,” February 3, 2006

SIGIR Report No. 05-025, “Management of the Commander’s Emergency Response Program for Fiscal Year 2005,” January 23, 2006

SIGIR Report No. 05-006, “Control of Cash Provided to South Central Iraq,” April 30, 2005

SIGIR Report No. 05-004, "Oversight of Funds Provided to Iraqi Ministries through the National Budget Process," January 30, 2005

AFAA

AFAA Report No. F2005-0011-FB1000, "Global War on Terrorism Funds Management," June 20, 2005

Appendix D. Disbursement Guidance

Federal Statutes and Regulations

Section 3325 title 31, United States Code, “Vouchers,” specifies that a disbursing officer should only disburse money when vouchers have been certified by an authorized certifying officer. Certified vouchers submitted to a disbursing official should include the taxpayer identifying number of each payee.

The Prompt Payment Act as implemented in 5 Code of Federal Regulations Part 1315 (2001), “Prompt Payment,” codifies the requirements that supporting documents must meet for proper payment.

The Federal Financial Management Improvement Act of 1996 states that each agency must implement and maintain financial management systems that comply substantially with Federal systems requirements and applicable Federal accounting standards.

Federal System Requirements

The Office of Federal Financial Management, “Core Financial System,” January 2006, states that audit trails must exist for transactions that are recorded as they move from the source through all document statuses. This requirement states that “adequate audit trails are critical to providing support for transactions and balances maintained by the core financial system.”

Federal Acquisition Regulation

FAR 2.101, “Definitions,” specifies the micro-purchase threshold for acquisitions as \$2,500; however, if determined by the head of the agency as being for contingency operations, the micro-purchase threshold outside the United States is \$25,000. It also defines the simplified acquisition threshold as \$100,000, except for acquisitions of supplies or services determined by the head of the agency to be for contingency operations. The threshold then increases to \$1,000,000 for contracts awarded and performed or for purchases made outside the United States.

FAR 13.306, “SF-44, Purchase Order-Invoice-Voucher,” describes the SF-44 as a multipurpose purchase order form designed primarily for on-the-spot, over-the-counter purchases of supplies and nonpersonal services while away from the purchasing officer or at isolated activities. The FAR allows for use of the SF-44 if the following conditions are met:

-
- the amount of the purchase is at or below the micro-purchase threshold, except for purchases made under unusual and compelling urgency in support of contingency operations;
 - the supplies or services are immediately available;
 - one delivery and one payment will be made; and
 - the use of the SF-44 is more economical and efficient than use of other simplified acquisition procedures.

FAR 18.201, “Contingency Operation,” states that the normal threshold for the use of the SF-44 is at or below the micro-purchase threshold; however, agencies may establish higher dollar limitations for purchases made to support a contingency operation.

FAR 32.905, “Payment Documentation and Process,” states that a payment will be based on receipt of proper invoice and satisfactory contract performance. This section of the guidance provides a list of 10 elements that a proper invoice must include. In addition, the guidance states that all invoice payments must be supported by a receiving report or other Government documentation authorizing payment.

Treasury Financial Manual

Volume 1, Part 2, Chapter 3100, “Instructions for Disbursing Officers’ Reports,” provides instructions for disbursing officers that perform disbursing operations. Disbursing offices are identified by a 3- or 4-digit code that must be shown on all forms.

Volume 1, Part 4, Chapter 2000, “Payment Issue Disbursing Procedures,” prescribes disbursing procedures. Certifying officers must sign the voucher, with their name typed or printed below the signature as evidence of certification. In addition, vouchers must identify all appropriations cited and their respective transaction amounts.

Defense Federal Acquisition Regulation Supplement

Defense Federal Acquisition Regulation Supplement 213.306, “SF-44, Purchase Order-Invoice-Voucher,” states that the micro-purchase limitation applies to all purchases, with the exception that purchases not exceeding the simplified acquisition threshold may be made for overseas transactions by contracting officers in support of a contingency operation or a humanitarian or peacekeeping operation.

DoD 7000.14-R, the “DoD Financial Management Regulation”

Volume 5, Chapter 11, “Disbursements,” describes a disbursement as a payment to an individual or organization for goods furnished or services rendered. The disbursement voucher is the authority for disbursing officers to make payments of Government obligations and is the source document for liquidation of obligations. Therefore, disbursement vouchers must contain complete and accurate data. In addition, the disbursing officers must only make disbursements from vouchers certified by authorized certifying officers. Cashiers must not make cash payments until they have positively identified the payee. The disbursement voucher must also indicate whether the disbursement was made by electronic funds transfer, U.S. Treasury check, cash, or as no check/voucher for transfer.

Volume 5, Chapter 21, “Disbursing Office Records,” provides guidance on the retention of disbursing office records. Disbursement vouchers must be retained for a minimum period of 6 years and 3 months.

Volume 10, “Contract Payment Policy and Procedures,” contains guidance regarding financial authorizations for contract payments and collections among the Office of the Secretary of Defense, the Military Departments, the Chairman of the Joint Chiefs of Staff, the Combatant Commands, the Inspector General of the Department of Defense, the Defense Agencies, and the DoD Components.

Department of the Army

Memorandum For Instruction, “Central Funding Standard Operating Procedures,” dated June 22, 2004, provides guidance to units operating in Iraq and Kuwait in support of Operation Iraqi Freedom. Specifically, it allows a disbursing officer, deputy disbursing officer, disbursing agent, or paying agent to receive and disburse cash for official business.

Defense Finance and Accounting Service

DFAS-IN Manual 37-100-06, “The Army Management Structure Fiscal Year 2006,” provides the codes and definitions for programming, budgeting, accounting, and manpower systems in use during fiscal year 2006 and subsequent years.

DFAS-IN Regulation 37-1, “Finance and Accounting Policy Implementation,” identifies roles and procedures for providing finance and accounting support to DFAS Indianapolis Operations customers. It also provides guidance on budgetary and proprietary accounting, fund control, financial reporting, and vendor pay and travel entitlements.

Appendix E. Results of Voucher Review

Compliance Criteria			
	Statutory Regulatory <u>Source*</u>	Number of Errors	Value of Errors (millions)
Total Noncompliance Vouchers- 662 for \$1,478.5 million			
Total Lacking Minimum Documentation for Payment Support- 125 for \$137.0 million			
Missing receiving report	C, H, J	23	32.5
Missing invoice	C	23	31.0
No certifying officer signature	A, E, F	5	41.7
No payee signature for receipt of cash	F	15	5.1
No contract number on invoice	C, H	31	18.7
SF-1034 voucher missing	F, G	2	0.3
SF-1034 voucher - contains complete accounting classification	E, F	3	1.3
SF-1034/SF-44 voucher - DSSN in the "brief" block	D, F	20	10.4
SF-1034 voucher - total amount shown with related accounting classification	E, F	4	6.7
Invoice - vendor name present	C, H	1	0.0
Invoice - item description	C, H	2	7.2
Invoice - quantity of goods or services rendered	C, H	6	16.7
Invoice - unit of measure	C, H	2	3.0
Invoice - total amount billed	C, H	5	12.0
Receiving report - contract number present	C, H	1	2.7
Receiving report - item description	C, H	2	7.2
Receiving report - unit of measure	H	1	0.3
Receiving report - quantity received	C, H	5	7.7
Receiving report - date of receipt	C, H	5	3.0
Receiving report - date of acceptance	C, H	5	3.0
Receiving report - signature of the receiving official	C, H	2	0.1
SF-44 – missing	B	1	0.0
SF-44 - ordered by signature	L	2	0.1
SF-44 - received by signature	L	2	0.7

Compliance Criteria (cont.)

	Statutory Regulatory <u>Source*</u>	Number of <u>Vouchers</u>	Value <u>(millions)</u>
SF-44 - same ordered by/received by signature	L	3	0.5
SF-44 - certifying officer signature	A, E, F,	1	0.0
SF-44 - payee signed for cash	F	9	0.8
Total Supported Payments Not Meeting Other Documentation Requirements- 537 for \$1,341.5 million			
No contact information on receiving report	C, H	394	1,185.6
No payment terms on invoice	C, H	343	333.6
No contact information on invoice	C, H	359	773.3
No taxpayer identification number on voucher	A, F	67	136.8
No foreign payee identification number on voucher	F	402	547.3
SF-1034 voucher - complete name of paying disbursing office	F	7	6.5
SF-1034 voucher - mailing address of the paying disbursing office	F	7	6.5
SF-1034 voucher - date the voucher was prepared	F	0	0.0
SF-1034 voucher - sub accounts of the same appropriation are grouped together	F	0	0.0
SF-1034 voucher - conversion rate to US dollars included for foreign currency disbursements	F	1	1.2
SF-1034 voucher - disbursement amount has been changed or altered	F	4	6.3
Invoice - vendor invoice number	C, H	54	14.9
Invoice - unit price	C, H	7	5.1
Invoice - tax identification number for U.S. companies	C, H	58	66.8
Invoice - banking information for electronic funds transfer	C, H	130	462.3
Invoice - original document (not a copy)	K	134	209.7
Invoice - submitted timely	K	13	23.5
Receiving report - contract/purchase order missing	I	38	88.2
Receiving report - vendor name	H	2	0.7
Receiving report - printed name of accepting or approving official	C, H	118	413.4
Receiving report – title of approving official	C, H	71	133.1
Misuse of SF-44	B	18	6.0
Method of disbursement not identified on voucher	F	19	45.8

Compliance Criteria (cont,)

***Statutory Regulatory Source**

A - 31 U.S.C. 3325

B - FAR 13.306

C - FAR 32.905

D - Treasury Financial Manual, volume 1, part 2, chapter 3100

E - Treasury Financial Manual, volume 1, part 4, chapter 2000

F - DoD FMR, volume 5, chapter 11

G - DoD FMR, volume 5, chapter 21

H - DoD FMR, volume 10, chapter 1

I - DoD FMR, volume 10, chapter 7

J - DoD FMR, volume 10, chapter 8

K - DoD FMR, volume 10, chapter 9

L - Central Funding Standard Operating Procedures

Appendix F. Payment Criteria Comparison

Comparison of DFAS Rome and DoD OIG Voucher Support Checklists	
Original DFAS Rome Payment Voucher Checklist	Items Needed to Support a Payment
<p style="text-align: center;"><u>Similarities</u></p> <ol style="list-style-type: none"> 1. Receiving Report 2. Invoice 3. Certifier’s signature 4. Disbursing Station Symbol Number 5. Contract number 6. Line of accounting <p style="text-align: center;"><u>Differences</u></p> <ol style="list-style-type: none"> 7. Contract (first or final payment) 8. Voucher number¹⁴ 9. Date 	<p style="text-align: center;"><u>Similarities</u></p> <ol style="list-style-type: none"> 1. Receiving Report 2. Invoice 3. Certifying officer signature (SF-1034) 4. SF-1034/SF-44 Voucher – DSSN in “Brief” block 5. Contract number on invoice 6. SF-1034 Voucher – Complete accounting classification <p style="text-align: center;"><u>Differences</u></p> <ol style="list-style-type: none"> 7. Payee signature for cash 8. SF-1034 Voucher 9. SF-1034 Voucher – Total amount with related accounting classification 10. Invoice – Vendor name present 11. Invoice – Item description 12. Invoice – Quantity of goods or services rendered 13. Invoice – Unit of measure 14. Invoice – Total amount billed 15. Receiving Report – Contract number 16. Receiving Report – Item description 17. Receiving Report – Unit of measure 18. Receiving Report – Quantity received 19. Receiving Report – Receipt date 20. Receiving Report – Acceptance date 21. Receiving Report – Receiving official signature 22. SF-44 23. SF-44 Ordered by signature 24. SF-44 Received by signature 25. SF-44 Signature same for ordered by and received by 26. SF-44 Certifying officer signature 27. SF-44 Payee signed for cash

¹⁴ To select the sample payments for this audit, the voucher number and date were required. As a result, all sampled items contained a voucher number and date. These data elements were not used as criteria for the payment support documentation or compliance review.

Appendix G. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition, Technology, and Logistics
Director, Acquisition Resources and Analysis
Under Secretary of Defense (Comptroller)/Chief Financial Officer
Deputy Chief Financial Officer
Deputy Comptroller (Program/Budget)

Department of the Army

Auditor General, Department of the Army
U.S. Army Corps of Engineers

Department of the Navy

Naval Inspector General
Auditor General, Department of the Navy

Department of the Air Force

Auditor General, Department of the Air Force

Other Defense Organizations

Director, Defense Finance and Accounting Service

Non-Defense Federal Organization

Office of Management and Budget

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations

Senate Subcommittee on Defense, Committee on Appropriations

Senate Committee on Armed Services

Senate Committee on Homeland Security and Governmental Affairs

House Committee on Appropriations

House Subcommittee on Defense, Committee on Appropriations

House Committee on Armed Services

House Committee on Oversight and Government Reform

House Subcommittee on Government Management, Organization, and Procurement,

Committee on Oversight and Government Reform

House Subcommittee on National Security and Foreign Affairs, Committee on Oversight and Government Reform

Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics Comments

Final Report Reference



ACQUISITION
TECHNOLOGY
AND LOGISTICS

OFFICE OF THE UNDER SECRETARY OF DEFENSE
3000 DEFENSE PENTAGON
WASHINGTON, DC 20301-3000

APR 25 2008

MEMORANDUM FOR PROGRAM DIRECTOR, DEFENSE FINANCIAL AUDITING SERVICE, DODIG

THROUGH: DIRECTOR, ACQUISITION RESOURCES AND ANALYSIS 7/8 4/28/08

SUBJECT: Response to DoDIG Draft Report D2006-D000FL-0208.000, "Internal Controls Over Out-of-Country Payments"

As requested, I am providing responses to the recommendations contained in the subject report.

Recommendation A.1. We recommend that the Under Secretary of Defense for Acquisition, Technology, and Logistics (USD (AT&L)) and the Under Secretary of Defense (Comptroller)/Chief Financial Officer (OUSD(C)) coordinate with the Office of Management and Budget (OMB) to resolve conflicting guidance in the Prompt Payment Act (PPA) regarding the documentation requirements for disbursements made in military contingency operations.

Response: Concur. We have discussed the inconsistency in 5 CFR 1315 with OMB and they have agreed to work with us as they assess their options to resolve the problem. We will continue to work with OMB and OUSD(C) toward a solution.

Recommendation B.1.a. We recommend that the USD(AT&L) and the OUSD(C) coordinate to obtain legal advice to determine the impact of contract clauses that require making interest payments and taking discounts on commercial payments for existing contracts in military contingency operations. Based on this, take appropriate actions to discontinue making interest payments and taking discounts for these contracts.

Response: Concur. The Department's Office of General Counsel (DGC) recently reviewed the applicable statutes and regulations and concluded that the Department has legal authority to pay interest penalties and retain early payment discounts. A copy of this legal opinion has been provided to your office. Based on that opinion, no action is required.

Recommendation B.1.b. We recommend that the USD(AT&L) and the OUSD(C) take appropriate action to resolve whether previous interest payments and discounts taken



Renumbered to B.1 and revised

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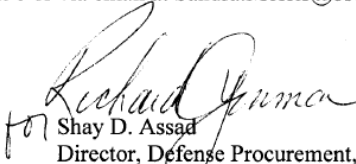
under the PPA for military contingency operations were justified or whether other actions are required to resolve the payments made.

Response: Concur. As discussed above, DGC reviewed the applicable statutes and regulations and concluded that the Department has legal authority to pay interest penalties and retain early payment discounts. Therefore, no action is required.

Recommendation B.2. We recommend that the Under Secretary of Defense for Acquisition, Technology and Logistics update the Federal Acquisition Regulation and the Defense Federal Acquisition Regulation Supplement to provide guidance that addresses the Prompt Payment Act exemption for payments related to military contingency operations. The guidance should specify the processes and contract clauses to be used in cases where exceptions to the Prompt Payment Act apply.

Response: Concur. After OMB resolves the inconsistencies in their regulations, we will update the Federal Acquisition Regulations (FAR) and the Defense FAR Supplement (DFARS) as necessary to be consistent with OMB's regulations.

If you have any questions regarding this memorandum, please contact my point of contact Ms. Sandra Morris, 703-602-0296 or via email at Sandra.Morris@osd.mil.


for Shay D. Assad
Director, Defense Procurement,
Acquisition Policy, and
Strategic Sourcing

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



COMPTROLLER

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

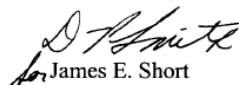
MEMORANDUM FOR PROGRAM DIRECTOR, DEFENSE FINANCIAL AUDITING
SERVICE, OFFICE OF INSPECTOR GENERAL,
DEPARTMENT OF DEFENSE

SUBJECT: Comments to Draft Audit Report, "Internal Controls Over Out-of-Country
Payments," (Project No. D2006-D000FL-0208.000)

This memorandum forwards the Under Secretary of Defense (Comptroller)
response to the subject draft DoD Inspector General report, dated February 11, 2008.
A copy of the response is attached.

As we have previously commented, we do not agree with the methodology used
by the Office of Inspector General, Department of Defense to estimate the projected
dollar amount of payments lacking missing information or supporting documentation.
The estimated dollar amount of payments not meeting all statutory or regulatory
requirements appears to give each type of error equal weighting and does not distinguish
between "critical" and "noncritical" errors. We believe that the projections are
misleading and invalid.

We appreciate the opportunity to respond to your draft audit report. My point of
contact is Ms. Audrey Clark. She can be reached by telephone at 703-695-9437 or
email at audrey.clark@osd.mil.


for James E. Short
Deputy Chief Financial Officer

Attachment:
As stated

DOD OIG DRAFT REPORT DATED FEBRUARY 11, 2008
PROJECT NO. D2006-D000FL-0208.000

“INTERNAL CONTROLS OVER OUT-OF-COUNTRY PAYMENTS”

OFFICE OF THE UNDER SECRETARY OF DEFENSE (COMPTROLLER)
(OUSD)(C) COMMENTS TO THE DOD OIG RECOMMENDATIONS

RECOMMENDATION A.1: We recommend that the Under Secretary of Defense for Acquisition, Technology, and Logistics (USD (AT&L)) and the Under Secretary of Defense (Comptroller)/Chief Financial Officer (OUSD(C)) coordinate with the Office of Management and Budget (OMB) to resolve conflicting guidance in the Prompt Payment Act (PPA) regarding the documentation requirements for disbursements made in military contingency operations.

OUSD(C) RESPONSE: Concur. We are engaged with both OMB and USD (AT&L) Defense Procurement and Acquisition Policy in resolving the issue. OMB has not currently provided an expected response date.

RECOMMENDATION A.2.a. We recommend that the OUSD(C) update the DoD 7000.14-R, “DoD Financial Management Regulation” (“DoDFMR”) to consolidate guidance that identifies the Federal Acquisition Regulation (FAR) and “DoDFMR” requirements to support commercial payments and address the deficiencies that are listed in Appendix E.

OUSD(C) RESPONSE: Partially Concur. We will update the “DoDFMR” as necessary to clarify financial management policy with respect to contingency operations, but will not reiterate acquisition policy, which is already contained in the FAR. The update, however, is contingent upon the resolution of the applicability of the PPA to contingency operations since many of the deficiencies cited in Appendix E use FAR Subpart 32.9 which “prescribes policies, procedures, and clauses for implementing Office of Management and Budget (OMB) prompt payment regulations at 5 CFR part 1315”. As noted in our response to Recommendation A.1, OMB has not currently provided an expected response date.

RECOMMENDATION A.2.b. We recommend that the OUSD(C) update the “DoDFMR” to clearly identify the appropriate uses and payment thresholds for the SF-44, as addressed in the FAR and the Defense Federal Acquisition Regulation Supplement (DFARS).

OUSD(C) RESPONSE: Partially concur. Identifying the appropriate uses and payment thresholds for the SF-44 are activities related to acquisition policy and are not under the purview of the OUSD(C). These recommendations should be redirected to USD (AT&L)

Attachment
Page 1 of 3

who has responsibility for acquisition policy. We will, however, update the “DoDFMR”, as necessary, to reflect any financial management policy changes caused by the subsequent issuance of SF-44 policy changes by USD (AT&L).

RECOMMENDATION B.1.a. We recommend that the USD(AT&L) and the OUSD(C) coordinate to obtain legal advice to determine the impact of contract clauses that require making interest payments and taking discounts on commercial payments for existing contracts in military contingency operations. Based on this, take appropriate actions to discontinue making interest payments and taking discounts for these contracts.

OUSD(C) RESPONSE: Concur. The Department’s Office of General Counsel recently reviewed the applicable statutes and regulations and concluded that the Department has legal authority to pay interest penalties and retain early payment discounts. A copy of this legal opinion has been provided to your office. As a result of this legal opinion, and in the absence of OMB guidance to the contrary, we will continue to pay the interest payments and take discounts in accordance with the terms and conditions of the existing contracts. Notwithstanding this, however, we are engaged with USD (AT&L) and OMB in resolving the inconsistency in OMB’s regulation regarding the applicability of the PPA to contingency operations. OMB has not currently provided an expected response date.

RECOMMENDATION B.1.b We recommend that the USD(AT&L) and the OUSD(C) take appropriate action to resolve whether previous interest payments and discounts taken under the PPA for military contingency operations were justified or whether other actions are required to resolve the payments made.

OUSD(C) RESPONSE: Concur. The USD (AT&L) requested the Office of General Counsel (OGC) opinion on this matter. As noted in our response to Recommendation B.1.a. above, the OGC reviewed the applicable statutes and regulations and concluded that the Department had legal authority to pay interest penalties and retain early payment discounts.

RECOMMENDATION B.3. We recommend that the OUSD(C) update the “DoDFMR” “ to provide guidance that addresses the PPA exemption for payments related to military contingency operations. The guidance should specify the processes to be used in cases where exceptions to the PPA apply.

OUSD(C) RESPONSE: Partially concur. As identified in our response to Recommendation A.1, we are engaged with USD (AT&L) and OMB in addressing the inconsistencies in the regulation with respect to the applicability of PPA to contingency operations. Once the issue is resolved, we will update the “DoDFMR” as necessary to clarify any related financial management policy with respect to contingency operations. OMB has not currently provided an expected response date.

Attachment
Page 2 of 3

RECOMMENDATION C.1: We recommend that the OUSD(C) update the "DoDFMR" Volume 12, Chapter 29 to specify documentation needed to support seized and vested asset payments to foreign government representatives. At a minimum, the policy should require documentation sufficient to provide an audit trail for such payments. The audit trail documentation should include supporting budget details and spending plans that can be reconciled to payment vouchers.

OUSD(C) RESPONSE: Partially concur. We are in the process of incorporating the July 31, 2003, OUSD(C) memorandum titled, "Appendices for Procedures Applicable to Vested and Seized Iraqi Property" into the "DoDFMR" as a permanent reference. We included a new section on records retention and disposition during contingency operations. We do not agree the audit trail documentation should include supporting budget details and spending plans that can be reconciled to payment vouchers. This is not a disbursing officer responsible. A budget and spend plan is a proposal based on assumptions for future events, that may change and may not be consistent with actual approved vouchers. Expected completion date is June 2008.

RECOMMENDATION C.2: We recommend that the OUSD(C) update "DoDFMR," Volume 12, Chapter 29 to require the reconciliation of funds that are paid to Coalition Partners.

OUSD(C) RESPONSE: Partially concur. In accordance with the "DoDFMR", Volume 5, paragraph 030402, all funds advanced to our coalition partners are reconciled when the coalition partner completes the assigned mission and turns in the DD Form 1081 (Statement of Agent Officer's Account) as a paying agent. Upon completion of the assigned mission, the paid vouchers, negotiable instruments, and any balance of funds are reconciled and returned to the responsible disbursing officer.

RECOMMENDATION C.3: We recommend that the OUSD (C) update "DoDFMR" Volume 12, Chapter 29 to establish policy on the use of Coalition Partners as paying agents that is suitable for use in future contingency operations with other foreign government representatives.

OUSD(C) RESPONSE: Partially concur. Paying agents must be U.S. citizens. The "DoDFMR", Volume 5, Chapter 2, provides the duties and responsibilities of paying agents. We will continue to require a waiver for all non-U.S. citizens acting as paying agents. Coalition forces are non-U.S. citizens, and may not be held pecuniary liable for losses of funds. A paying agent is an agent to the disbursing officer, and as such, the disbursing officer remains pecuniary liable for all public funds under his/her control. We will continue to require that coalition forces reconcile funds advanced to them in the same manner as U.S. citizens as stated in the "DoDFMR", Volume 5, Chapters 2 and 5.

Attachment
Page 3 of 3

Department of the Army Comments



REPLY TO
ATTENTION OF

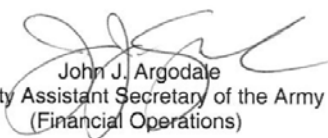
DEPARTMENT OF THE ARMY
OFFICE OF THE ASSISTANT SECRETARY OF THE ARMY
FINANCIAL MANAGEMENT AND COMPTROLLER
109 ARMY PENTAGON
WASHINGTON DC 20310-0109

MAR 24 2008

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDITING, OFFICE OF THE DEPARTMENT OF DEFENSE INSPECTOR GENERAL, 400 ARMY NAVY DRIVE, ARLINGTON, VIRGINIA 2202

SUBJECT: DoDIG Draft Report for the Audit of Internal Controls Over Out-of-Country Payments (Project No. D2006-D000FL-0208.000)

1. We appreciate the opportunity to comment on the subject draft audit report and partially agree with your salient findings.
2. The draft report appears to be inconsistent with DoD policy. While the report cites lack of compliance with the Prompt Payment Act as the basis of its findings, it also indicates the Prompt Payment Act does not apply to out-of-country payments. It is recognized that there were administrative errors, the audit trail is difficult to follow, and a small percentage of vouchers require follow-up due to critical deficiencies such as a missing payee signature.
3. If the auditors had been able to travel to the theater to follow the appropriate audit trails or to Fort McCoy to observe the training being given to deploying units, the audit report would be more informative and identify specific areas of concern. We will work with the Army Audit Agency to perform a more robust audit of payments made in theater and pre-deployment training in order to more accurately identify internal control issues and corrective actions.
4. Specific responses to the draft recommendations are attached. My point of contact for this matter is Mr. G. Eric Reid at eric.reid@dfas.mil or telephone (317) 510-2223.


John J. Argodale
Deputy Assistant Secretary of the Army
(Financial Operations)

Attachment

DoDIG Project No. D2006-D000FL-0208.000

Audit of Internal Controls over Out-Of-Country Payments

Department of the Army Comments to the Recommendations

Recommendation A-3: We recommend that the Assistant Secretary of the Army (Financial Management and Comptroller):

- a. Review the 125 commercial payments that were not properly supported and, if the error cannot be resolved, determine whether a loss of funds investigation or other investigative action, such as a payment recovery audit, is required to ensure the payment was not an improper payment.
- b. Require that the certifying officer at an Army finance office complete a standard checklist of required commercial payment support elements developed from the Federal Acquisition Regulation and the DoD 7000.14-R, "DoD Financial Management Regulation" before the payment voucher is forwarded to the appropriate disbursing and accounting offices.
- c. Develop an integrated training approach providing adequate and timely training in disbursing, vendor pay, and accounting operations to finance personnel deployed to contingency disbursing stations.
- d. Address the internal control deficiencies identified in this report in the Annual Statement of Assurance as material weaknesses.

Army Response: Partially concur.

- a. The Army has initiated review of commercial payments that were not properly supported based on applicable laws and regulations. For those vouchers which a reasonable assurance of payment to the vendor cannot be ascertained, a formal loss of funds investigation will be initiated.
- b. The Army will revise the current checklist provided to the deployed finance offices once a determination of revised requirements under the exemption from the prompt payment act and employer identification number requirements is finalized by OSD. Deployed Army finance offices will be directed to use the checklist.
- c. The Army already has an integrated training program including disbursing and vendor pay for units deploying to theater. This program is under continual review and improvement.
- d. The complex audit trails related to vendor payments made in a contingency theater of operations will be identified as a material weakness in the next Army Annual Statement of Assurance.

Recommendation A.4: We recommend that the Assistant Secretary of the Army (Financial Management and Comptroller) and the Director, Defense Finance and Accounting Service establish a formal agreement that clarifies each organization's distinct responsibilities to ensure proper accountability for commercial payment vouchers.

Army Response: Concur. The Army will work with DFAS to update the existing standard operating procedures and formalize it in a memorandum of agreement. Completion of this is dependent on the issuance of revised OSD guidance covering the exemption from the prompt payment act and employer identification number requirements.

Defense Finance and Accounting Service Comments



DEFENSE FINANCE AND ACCOUNTING SERVICE
8899 EAST 56 TH STREET
INDIANAPOLIS, INDIANA 46249

MAR 2 5 2008

DFAS-JJ/IN

MEMORANDUM FOR PROGRAM DIRECTOR, DEFENSE FINANCIAL AUDITING
SERVICE, OFFICE OF THE INSPECTOR GENERAL,
DEPARTMENT OF DEFENSE

SUBJECT: DFAS comments on DoDIG Draft Report, "Internal Controls Over Out-of-Country
Payments," Project No. D2006-D000FL-0208.000, dated February 11, 2008

Per your request please see the DFAS management comments at TAB A, to
recommendation A4 of the subject draft audit report. Recommendation A4 was completed on
October 15, 2007.

In response to the preliminary audit results, we implemented a number of process
changes. The initial results identified a number of administrative requirements not included in
the supporting documentation for Army payments in contingency operations. Improvements
were also needed to controls over in-theater supporting documentation warehoused at the
Defense Finance and Accounting Service (DFAS), Rome, New York. As a result, the Army and
DFAS made the following improvements for contingency payments:

- increased physical controls over documents;
- implemented a checklist identifying required supporting documentation; and
- established a Balanced Scorecard metric to gauge the effectiveness of the improved
controls.

The Office of the Under Secretary of Defense (Comptroller) published a memorandum,
subject: "Certified Commercial Payments in Contingency Operations," on September 14, 2007,
emphasizing the typical requirements for proper payments in contingency operations. The
Department is updating the DoD Financial Management Regulation to clearly define
requirements in contingency operations. We incorporated these changes in training provided to
in-theater and deploying units. The Army will also incorporate the changes when conducting
ongoing and future training.

Additionally, DFAS and Army undertook the actions below to improve processes and
reduce the burden on units in Iraq and Kuwait.

- To enhance financial management, DFAS established in-theater support cells to provide
accounting, reconciliation, financial reporting, fund execution, joint review support, and
training to finance units.

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- The support cells are assessing in-theater workload to identify financial functions to transfer to the United States to allow soldiers to focus on military missions and improve the efficiency of financial operations supporting the Global War on Terror.
 - We are implementing document imaging to improve efficiency; reduce costs associated with document transfer, storage and retention; and reduce risk to soldiers transporting documents in-theater of operations.

Direct any questions to Tom Roberts at 317-510-2133 or tom.roberts@dfas.mil.



Edna J. Knight
Deputy Director, Standards
Standards & Compliance

Attachments:
As stated

cc:
Department of the Army
Office of the Under Secretary of Defense (Comptroller)

DFAS comments on DoDIG Draft Report, "Internal Controls Over Out-of-Country Payments", Project No. D2006-D000FL-0208.000, dated February 11, 2008

Recommendation A4: We recommend that the Assistant Secretary of the Army (Financial Management and Comptroller) and the Director, Defense Finance and Accounting Service establish a formal agreement that clarifies each organization's distinct responsibilities to ensure proper accountability for commercial payment vouchers.

DFAS Response: Concur. Memorandum of Agreements were executed for retrogrades from Kuwait and Qatar and U.S. Army Central Command Support Teams. We will continue working with the Army to establish agreements clarifying each organization's responsibilities as additional initiatives are executed to support the Army commands in contingency operations.

Completion Date: October 15, 2007

TAB A

U.S. Army Corps of Engineers Finance Center Comments

Final Report
Reference



DEPARTMENT OF THE ARMY
U.S. ARMY CORPS OF ENGINEERS
441 G ST. NW
WASHINGTON, D.C. 20314-1000

CEIR

21 April 2008

MEMORANDUM FOR Department of Defense Inspector General, Office of the Assistant
Inspector General for Auditing, 8899 East 56th Street, Indianapolis, Indiana 46249-7501

SUBJECT: Revised USACE Response - Report on Internal Controls Over Out-of-Country
Payments (Project No. D2006-D000FL-0208.000)

1. References:

- a. DoDIG Memorandum 11 Feb 08, subject as above.
- b. CEIR Memorandum 17 March 2008, subject as above.

2. This Revised USACE Response to the subject draft report replaces the response dated
17 March 2008 (reference 1.b.).

3. The subject report contains no recommendations to the U. S. Army Corps of
Engineers. Nevertheless, there were statements in Section D, Miscellaneous Payments of
the report that reflected negatively on USACE which require clarification and comment.

Page 23 – Section D, Miscellaneous Payments:

(1) The second paragraph under "Iraqi Funds" states there is still \$10.7M in
debt owed to the U.S. Government by the Iraqi Government but the final paragraph
under Section D, Management Actions, references the settlement of \$9.2 million
delinquent debt owed by the Government of Iraq. The actual current delinquent
amount owed by the Government of Iraq is \$9.2 million as the result of a credit of
\$1.5M applied to an open bill which reduced the debt from \$10.7 million to the current
amount of \$9.2 million.

(2) The second paragraph of "Wire Transfers" states that "The Corps
Finance Center should have contacted or sought guidance from the Joint Area Support
Group and the USD(C)/CFO to identify a resolution for the funds so that they could have
been put to better use." The USACE Finance Center contacted the Joint Area Support
Group, Project Contracting Office, and Joint Contracting Command - Iraq/Afghanistan
multiple times with no results and copies were provided to the DoDIG auditors. Also,
during this time the USACE unpaid bills began to surface so there was no further

Revised
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CEIR 21 April 2008
SUBJECT: Revised USACE Response - Report on Internal Controls Over Out-of-Country
Payments (Project No. D2006-D000FL-0208.000)

aggressive action to return funds pending resolution of whether the excess funds could be used to offset the unpaid bills.

(3) We take exception to the final paragraph of "Wire Transfers" which states, "By leaving the funds in a suspense account and not returning them to the CPA, the Corps Finance Center delayed the availability of funds for assisting the Iraqi people in the reconstruction of Iraq." These funds could not be returned to the CPA which no longer existed and the USACE Finance Center placed them in suspense. This was a prudent action to keep the funds visible/reviewed until proper disposition could be determined. USACE continued to provide service and support to the Iraqi people through its reconstruction projects while still holding \$9.2 million in debt from the Iraqi government.

4. On 1 April we received word from DoDIG that our original response did not address the Potential Monetary Benefits presented in Appendix G of the subject report. Our comments are provided below:

There was never any discussion of Appendix G, Summary of Potential Monetary Benefits, with the DoD IG auditors nor were any of their recommendations directed to USACE. We have e-mail message from DoD Comptroller staff to allow applying \$5.7M of Iraq Seized Assets advanced funds being held by the USACE Finance Center in a suspense account to liquidate delinquent DFI accounts receivable from the government of Iraq (attached). Formal written response from the DoD Comptroller is currently being prepared. Based on this we can concur.

5. Any questions should be referred to the undersigned, 202-761-8518.

Atch
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DONNA F. JOHNSON
Acting Chief, Audit Executive
HQ, USACE Internal Review Office

CF:
CEMP
CERM
CEGRD
CEUFC

Team Members

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Inspector General Department of Defense

