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Accounting and Information  
Management Division

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April 3, 1997

Mr. Charles R. Coffee, Director  
Defense Finance and Accounting  
Service, Columbus Center  
P.O. Box 182317  
East 5th Avenue  
Columbus, Ohio 43218-2317

Subject: DOD Problem Disbursements: Contract Modifications Not Properly  
Recorded in Payment System

Dear Mr. Coffee:

The Department of Defense (DOD) has identified payment and accounting errors related to contract modifications as a significant cause of problem disbursements. Contract modifications authorize and specify changes to contracts and can, among other things, increase and decrease amounts to be paid and change accounting lines from which payments should be made. Therefore, such modifications must be recorded properly in the payment systems in a time frame that is consistent with both the effective dates of the modifications and related contract payments.

We have an ongoing review of 175 selected long-term contracts for which recurring payments are made by the Defense Finance and Accounting Service, Columbus Center. These contracts were associated with large amounts of problem disbursements. As a part of this review, we evaluated those contracts' modification files. We advised you and your staff during our March 13, 1997, briefing that our preliminary analysis raised significant concerns as to whether (1) modifications were being input properly into the Center's payment system in a timely manner and (2) information from the modification files was being used to effectively manage the input process. The purpose of this letter is to outline our concerns in three key areas: missing modification numbers, delayed modification input, and duplicate modification input. The data in this letter were derived from the Columbus Center's modification files, and we did not

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independently verify or audit the data. We performed our work from June 1996 to March 1997 in accordance with generally accepted government auditing standards.

#### MISSING MODIFICATION NUMBERS

To effectively control and account for contract modifications, each new modification is to be assigned a unique number in sequential order. The Center's modification records contain a file identifying modification numbers missing from the sequences that have been input into the payment system. According to your staff, this file is to be used as a basic internal control to follow up on unrecorded modifications to help ensure timely input. For the 175 selected contracts in our review, we found that the Center's missing modification file identified over 2,400 missing modification numbers, including some that had been missing for years. For example, one modification number had been in the missing modification file—meaning the modification had not been received or cancelled—since July 23, 1992. Another modification number had been in the file since November 15, 1993. Columbus Center personnel told us that no follow-up had been done to determine why these numbers were missing.

According to your staff and consistent with our observation of the Center's modification input process, the missing modification file is not being used to follow up on unrecorded modifications. One division director said the files were not used because staff did not have time to follow up. We were also told that it was not unusual for modification numbers to be missing from sequences because personnel who prepare modifications may skip or not use a number. However, as your staff noted, clearing such unused numbers from the missing file should not be difficult and would serve as an important control for ensuring that all actual modifications are accounted for and entered into the payment system. According to personnel responsible for modification input and problem correction, modifications that have not been entered into the system are often not detected under current processes until a payment problem occurs.

#### DELAYED MODIFICATION INPUT

Because the timely input of contract modifications is necessary to ensure accurate and timely payment of invoices, we compared the modification effective dates with input dates over a 1-year period for 25 of the more frequently modified contracts from the 175 selected contracts. We found that for 17 of the 25 contracts, modifications, on average, were input 30 days or more after their effective dates. For 10 of the 25 contracts, the average time between the

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effective modification dates and the input dates exceeded 100 days. Modifications for one contract were input to the Columbus Center's contract payment system an average of about 260 days after their effective dates.

In addition, over 5,200 modifications related to our selected 175 contracts had been input out of sequence with respect to their effective dates. This means that modifications with later effective dates—which can change the impact of preceding modifications—were input first. For example, a modification on one contract with an effective date of September 8, 1988, was input to the Center's payment system on September 22, 1988, whereas another modification to the same contract with an earlier effective date of September 7, 1988, was not input until April 26, 1994.

Although we did not analyze the causes for input delays, we did note that in many cases Columbus Center did not receive the modifications from the responsible contract officials within 30 days of their effective dates. For example, one modification with an effective date of November 15, 1995, was reported as received by the Columbus Center on September 13, 1996, and was input into the system 2 days later.

#### DUPLICATE MODIFICATION INPUT

Finally, we identified 146 numbered modifications that had been entered more than once into the Center's system. For example, a contract modification with an effective date of November 30, 1990, was entered on January 8, 1991, and again on May 1, 1991. If a modification involves contract funding, duplicate entries would result in inappropriate increases or decreases to obligation amounts. If an obligation is inappropriately entered twice, the obligations for the contract are overstated, and overpayments could result. Conversely, if an obligation is inappropriately decreased, funding may be inadequate to pay proper invoices. In either case, additional audit and/or reconciliation work would be necessary to resolve problems caused by duplicate entries.

Your staff reviewed payment system records for selected modifications that were recorded as duplicates in the modification files and confirmed that some had been entered twice into the contract payment records. However, they stated that other modifications that had been identified as duplicates in the modification files resulted from the transfer of contract records between the Center's directorates but had not been entered twice into the contract payment records.

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In responding to the matters discussed in this letter, DOD officials advised us that actions are under way to improve the accuracy and timeliness of modification input. They said that DOD is testing the feasibility of direct input of modifications by administrative contracting offices rather than by Columbus Center personnel. Also, they said DOD has proposed an edit change to the contract payment system that will help prevent modifications from being entered out of sequence. This proposed change would involve the creation of a suspense file in which out-of-sequence modifications will be held for manual review to determine appropriate application. These actions indicate DOD's recognition of the continuing need to have adequate control over the input of modifications.

We are not making specific recommendations at this time because we are continuing our more comprehensive analysis of actions that could be needed to more effectively manage disbursement problems on existing contracts. However, because you and your staff indicated an intent to follow up on the modification issues discussed during the briefing, we are providing this letter at this time. If you desire, we will provide more specific information regarding the results of our analysis. We would also appreciate being informed of any actions taken in response to this information to improve management of contract modifications.

We are sending copies of this letter to the Under Secretary of Defense (Comptroller) and the Director, Defense Finance and Accounting Service. Copies will be available to others upon request. If you have questions or comments on matters discussed in this letter, please contact me at (202) 512-9095. The major contributors to this letter were David Childress, Benjamin W. Smith, Jr., Evert A. Stevens, and Donald L. Ficklin.

Sincerely yours,

  
for Lisa G. Jacobson  
Director, Defense Financial Audits

(918872)

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