Report No. D-2007-061 March 1, 2007

Inspector General

United States Department of Defense

Defense Finance and Accounting Service Dayton Network Compliance with the Prompt Payment Act

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Acronyms

CFR	Code of Federal Regulations
DFAS	Defense Finance and Accounting Service
EDM	Electronic Document Management
IAPS	Integrated Accounts Payable System

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

March 1, 2007

MEMORANDUM FOR DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE, HEADQUARTERS
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE, DAYTON
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE, COLUMBUS
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE, LIMESTONE

SUBJECT: Report on Defense Finance and Accounting Service Dayton Network Compliance with the Prompt Payment Act (Report No. D-2007-061)

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. The Defense Finance and Accounting Service Indianapolis comments were partially responsive. We request additional comments on Recommendations 1.a, 1.b.3, 1.c, and 2. We request that the Director, Corporate Reporting Standards and Compliance, Defense Finance and Accounting Service Indianapolis provide comments on Recommendations 1.a, 1.b.3, 1.c, and 2 by April 2, 2007.

If possible, please send management comments in electronic format (Adobe Acrobat file only) to Audcolu@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 James L. Kornides at (614) 751-1400, ext. 211 or Mr. Mark Starinsky at (614) 751-1400, ext. 231. See Appendix B for the report distribution. The team members are listed inside the back cover.

By direction of the Deputy Inspector General for Auditing:

Paul J. Granetto, CPA
Assistant Inspector General and Director
Defense Financial Auditing Service

Department of Defense Office of Inspector General

Report No. D-2007-061 **March 1, 2007**
(Project No. D2006-D000FJ-0178.00)

Defense Finance and Accounting Service Dayton Network Compliance with the Prompt Payment Act

Executive Summary

Who Should Read This Report and Why? DoD personnel responsible for processing payments in accordance with the Prompt Payment Act should read this report. It discusses internal controls that ensure payments are made on time and that appropriate interest is paid.

Background. On October 3, 2005, the Defense Hotline received a complaint that the Defense Finance and Accounting Service (DFAS) offices in Dayton, Omaha, San Bernardino, and Orlando were not paying invoices in accordance with the Prompt Payment Act. The complainant alleged that in certain instances the DFAS offices were not properly calculating the payment due date for payments.

The Prompt Payment Act of 1998, section 3903, title 31, United States Code, requires Federal agencies to pay bills on a timely basis and to pay interest penalties when payments are made late.

This report uses the term DFAS Dayton Network to collectively refer to the DFAS payment offices located in Dayton, Omaha, Orlando, and San Bernardino. DFAS Dayton Network records indicated that its Vendor Pay Product Line paid about $7.6 billion to contractors from April 2005 through March 2006.

Results. We substantiated the allegation that the DFAS Dayton Network did not always pay invoices in accordance with the Prompt Payment Act. For 61 of the 75 invoices in our judgmental sample, the offices in the DFAS Dayton Network did not use the proper payment information, including the receipt date and the proper payment terms that are required by the Prompt Payment Act. As a result, the DFAS Dayton Network offices made $91,673 of interest errors on 42 of those 61 sample invoices. The errors were related to interest lost when DFAS Dayton Network made payments earlier than allowable by the Prompt Payment Act and when it overpaid or underpaid the interest due to the contractor for the late payment. There is an additional risk that DFAS Dayton Network will continue to overpay and underpay interest to contractors and will continue to pay invoices earlier than allowable under the Act, which can result in further interest lost to the Government. Responsibility for the Vendor Pay Product Line is being transferred to DFAS Columbus and DFAS Limestone in 2008 as part of the Base Realignment and Closure study. To comply with the Prompt Payment Act, those offices needed to provide training to their personnel and needed to create detailed formal guidance for technicians to ensure that they comply with the Prompt Payment Act. See the Finding section of the report for the detailed recommendations.

The DFAS Dayton Network's internal controls were not adequate. We identified material management control weakness in the processing of payments in compliance with the Prompt Payment Act.

Management Comments and Audit Response. The Director, Corporate Reporting Standards and Compliance, Defense Finance and Accounting Service Indianapolis concurred and planned to update the Integrated Accounts Payable System (IAPS) Student Guide to incorporate the Database Extension and Restructure changes and ensure that the Student Guide is available to all paying offices that process IAPS payments. In addition, the Director planned to provide training to all incoming personnel and personnel recommended for training by management. In general, the comments were responsive; however, we request that the Director, Corporate Reporting Standards and Compliance, Defense Finance and Accounting Service Indianapolis provide additional comments regarding his proposed actions to update the Student Guide to include adequate instructions for processing and returning IAPS invoices and to provide training to IAPS technicians and certifying officers. We request that the Director, Corporate Reporting Standards and Compliance, Defense Finance and Accounting Service Indianapolis provide comments on the final report by April 2, 2007. See the Finding section of the report for a discussion of management comments and Management Comments section of the report for the complete text of the comments.

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Background

On October 3, 2005, the Defense Hotline received a complaint that the Defense Finance and Accounting Service (DFAS) offices in Dayton, Ohio; Omaha, Nebraska; San Bernardino, California; and Orlando, Florida, were not paying invoices in accordance with the Prompt Payment Act. The Complaint alleged that in certain instances those DFAS offices were not properly calculating the payment due date for invoices.

The Prompt Payment Act (the Act) of 1998, section 3903, title 31, United States Code, requires Federal agencies to pay bills on a timely basis and to pay interest penalties when payments are made late.

This report uses the term DFAS Dayton Network to refer to the DFAS payment offices located in Dayton, Omaha, Orlando, and San Bernardino. DFAS Dayton Network records indicated that it paid about $7.6 billion to contractors from April 2005 through March 2006 that was subject to the Act.

The 2005 Base Realignment and Closure resulted in DFAS Dayton, Omaha, Orlando, and San Bernardino closing by early 2008. As a result, in June 2006, the DFAS Dayton database was realigned to DFAS Columbus and DFAS Limestone, with each DFAS location assuming responsibility for portions of the database.

When the Dayton, Omaha, Orlando, and San Bernardino centers close, the workload will transfer to either DFAS Columbus or DFAS Limestone based on the customer these locations support.

Objectives

Our audit objective was to evaluate whether DFAS offices located in Dayton, Omaha, Orlando, and San Bernardino were making payments to contractors in accordance with the Prompt Payment Act. See Appendix A for a discussion of the scope and methodology.

Review of Internal Controls

We identified a material internal control weakness for the DFAS Dayton Network as identified by DoD Instruction 5010.40, "Managers' Internal Control (MIC) Program Procedures," January 4, 2006. The DFAS Dayton Network did not have proper and adequate guidance and training for processing invoices in compliance with the Act. Implementing the recommendations will improve the DFAS Dayton Network compliance with the Act. A copy of the report will be provided to the senior officials responsible for internal controls in the DFAS Dayton Network.

Integrated Accounts Payable System Prompt Payment Act Controls

We substantiated the allegation that the DFAS Dayton Network did not always pay invoices in accordance with the Prompt Payment Act. For 61 of the 75 invoices in our judgmental sample, the offices in the DFAS Dayton Network did not use the proper payment date (such as receipt date) or the proper payment terms that were required by the Act. The noncompliance occurred because the DFAS Dayton Network did not provide necessary formal training to all employees who needed it and, in certain instances, adequate detailed written procedures did not exist. As a result, the DFAS Dayton Network offices made $91,673 of interest errors on 42 of those 61 sample invoices. The errors were related to interest lost when DFAS Dayton Network made payments earlier than allowable by the Act and when it overpaid or underpaid the interest due to the contractor for the late payment. There is an additional risk that DFAS Dayton Network will continue to overpay and underpay interest to contractors and will continue to pay invoices earlier than allowable under the Act, which can result in further interest lost to the Government. Responsibility for the Vendor Pay Product Line is being transferred to DFAS Columbus and DFAS Limestone in 2008 as part of the Base Realignment and Closure study. To comply with the Act, those offices need to provide training to their personnel and need to create detailed formal guidance for technicians.

Workings of the DFAS Dayton Network Payment Operation

Using Integrated Accounts Payable System. The DFAS Dayton Network used the Integrated Accounts Payable System (IAPS), an automated commercial pay system, to account for and process payments submitted to commercial vendors. For all invoices DFAS Dayton Network receives, IAPS automatically calculates the payment due date based on contract terms entered by technicians. The system also schedules the payment date, calculates any interest penalty due to the contractor, and processes the final payment data. IAPS electronically sends the payment processing data, including any interest penalties due, to the disbursing office for payment of the invoice.

Each DFAS Dayton Network center had three primary sections that are involved in making invoice payments: the Tier II, Accounts Payable, and Certification sections. Tier II was responsible for scanning, indexing, and properly routing documents through the Electronic Document Management (EDM) system. Accounts Payable was responsible for manually entering all obligation, invoice, and receiving report information into IAPS. Accounts Payable was also responsible for forwarding the EDM documents to Certification when an invoice is ready for payment. Certification was responsible for reviewing and certifying payments and forwarding them to Disbursing.

Universe of Invoice Payments. DFAS Dayton Network paid 120,660 invoices totaling $7.6 billion from April 1, 2005, through March 31, 2006. According to DFAS Dayton Network, all of the invoices were subject to the provisions of the Act and were processed through IAPS. The IAPS database contained payment records with the contract number, invoice number, invoice receipt date, payment date, contractor name, and payment amount. DFAS Dayton Network maintained data fields indicating whether they earned a discount or paid interest on the invoice.

Universe of Improper Invoices. DFAS Dayton Network also provided a spreadsheet of 32,495 invoices that they stated had been returned to either the buying activity or the contractor from April 1, 2005, through March 31, 2006. DFAS Dayton Network provided the contract number, date the invoice was scanned into the EDM system, and the date it was sent back. DFAS Dayton Network ran a report in EDM to obtain the spreadsheet listing all documents it coded as "RTV" (returned to vendor).

Of the 32,495 returned invoices, 27,241 were subject to the Act. The remaining 5,254 invoices were not subject to the Act because the payments were primarily for items such as moving expenses or grants.

Audit Sample. We selected a judgmental sample of 75 invoice payments, totaling $370 million, of the 120,660 invoice payments. The judgmental sample represented 5 percent of the total disbursements and less than .01 percent of the total invoices. We primarily selected high-dollar invoices for review. In selecting the sample, we ensured an even distribution of payments made before, during, and after the standard required payment period (that is, 25 invoices paid less than 23 days after the invoice receipt date, between the 23rd and 30th day, and after the 30th day). We also ensured that 30 invoices that DFAS Dayton Network included on the "RTV" spreadsheet of invoices returned to the buying activity or contractor as improper were included in our 75 sample invoice payments.

DFAS Policies and Procedures. DFAS Denver has developed a policy guide for IAPS users called the Vendor Payment Desktop Guide. DFAS Columbus has developed the IAPS Guide (a training guide).[1] Both of these guides provide instructions on how to enter data into IAPS. In addition, DFAS Denver Instruction 7077.7-M provides a description of IAPS codes.

Compliance with Requirements of the Prompt Payment Act

The DFAS Dayton Network did not comply with certain elements of the Prompt Payment Act. Specifically, the DFAS Dayton Network did not always select the receipt date or the payment terms specified by the Act. In addition, the DFAS Dayton Network did not always properly calculate the payment due date or

[1] The IAPS Guide was not available for use by the DFAS Dayton Network for the invoices reviewed. We reviewed the manual to determine whether it included detailed procedures to process invoices in accordance with the Act.

interest as required by the Act. Also, the DFAS Dayton Network did not follow DFAS Denver policy related to controls over the handling of improper invoices. Often errors occurred on the same invoice and the total number of errors that occurred was more than the 75 sample invoice payments. The table shows a summary of the errors.

Result of Testing

Category	Number of Invoices with Error*
No Errors Detected	14
Used Incorrect Payment Terms	34
Improperly Determined Invoice Receipt and Acceptance Dates	33
Did Not Factor in Return of Invoice when Calculating the Due Date	18
Inconsistent Work on Returning Improper Invoices	37

*Some invoices had multiple errors. Therefore, the total number of errors is higher than the sample size.

Payment Terms. According to the Prompt Payment Act, 31 U.S.C. 3903 (a) (1) the required payment terms are (a) the date payment is due under the contract for the item of property or service provided, or (b) 30 days after a proper invoice for the amount due is received if a specific payment date is not established by contract. The DFAS Dayton Network personnel used incorrect payment terms for 34 of the 75 sample invoices.

Payment Due Date. DFAS Dayton Network personnel processed 21 sample IAPS invoices that had IAPS payment due dates of less than 30 days even though the contract terms listed either 30 days or were silent on the payment terms. For 7 of the 21 invoices, DFAS Dayton Network used payment terms of 14 days without adequate support. For two other invoices, DFAS Dayton Network used 3 and 5 days as the payment due date. These had annotations that the invoices had previously been returned to the buying activity and that payment should occur as quickly as possible. For the remaining 12 invoices, DFAS Dayton Network selected the payment terms listed on the front of the contract in the box titled "Discount for Prompt Payment." However, the Federal Acquisition Regulation clauses in the body of the contract specify that the payment due date is 30 days, which takes precedence over the payment terms on the front of the contract. An incorrect payment due date could result in either an early payment

to the contractor (and subsequent interest lost to the Government), an overpayment, or an underpayment of interest to the contractor.

For 16 of the 21 invoices, DFAS Dayton Network had entered the "Prompt Payment Indicator" code in IAPS as "B," so interest accrued only when payments were made more than 30 days after receipt, regardless of the payment due date. Because DFAS Network entered a payment due date that was earlier than the required contractual due date of 30 days while still ensuring that interest was not paid until the 31st day, DFAS Dayton Network circumvented the Act's cash management requirement which states that interest begins to accrue on the day after the payment due date.

Neither the IAPS Guide nor the Vendor Payment Desktop Guide contained any guidance on how to determine the proper payment due date. The IAPS Guide only states that the MAX-PAY-DAYS field needs to be entered with the number of days to pay. However, it does not provide detailed guidance to the technicians on where to look in the contract to determine what the payment due date should be. Detailed written guidance will ensure that the proper payment date is selected based on the contract. An incorrect payment due date could result in either interest lost to the Government or an underpayment of interest.

DFAS Dayton Network also did not have adequate written guidance or policy to correctly determine the Prompt Payment Indicator. Specifically, the Vendor Payment Desktop Guide had no guidance on entering the Prompt Payment Code and the IAPS Guide did not include a description of code B or how to determine what code should be used. DFAS Denver Instruction 7077.7-M states that Prompt Payment Indicator code B should be entered for bank payments. However, none of the sample items selected represented bank payments. A few DFAS Dayton Network technicians stated that their understanding was that code B should be entered when the payment terms were less than 30 days to allow for the earlier payment, but to prevent interest from accruing until the 30th day.

The Vendor Payment Desktop Guide and the IAPS Guide need to be updated to allow only the use of code B for bank payments, as the Act does not permit two "due dates"—one for payment and one for calculating interest. By using two due dates, DFAS Dayton Network is circumventing one of the two parts of the Act (early payment or interest calculation).

Subject to the Act. There were 15 sample invoices that DFAS Dayton Network had coded as exempt from the Act by entering an "E" in the Prompt Payment Indicator code in IAPS.[2] However, the only invoices exempt from the Act are contract financing payments, payments for emergencies, utility payments, and commodity credit corporation payments. None of the 15 sample invoices fit into any of these categories. One sample invoice was coded as exempt from the Act, but when the contractor requested interest payment for the invoice that was over 100 days late, DFAS Dayton Network paid the interest. An invoice incorrectly coded as exempt could result in an underpayment of interest to the contractor.

[2] Two of these sample payments also had incorrect payment terms entered into IAPS.

DFAS Dayton Network did not have adequate written guidance or policy on correctly determining the Prompt Payment Indicator. Specifically, the Vendor Payment Desktop Guide had no guidance on entering the Prompt Payment Code and the IAPS Guide only stated that "E" meant that the payment is exempt from the Act provision. There was no detailed guidance for the technicians to determine if a contract is exempt from the Prompt Payment Act. Additional detailed guidance is needed to ensure that only those invoices exempt from the Act are coded as such.

Determination of the Date of the Proper Invoice. DFAS Dayton Network entered 33 of the 75 sample invoices incorrectly in IAPS. The Act states that the payment terms start on the day the Government receives a proper invoice. It further defines that a proper invoice is received on the later of (1) the date the designated Government office receives a proper invoice or (2) the date the designated Government office accepts the goods or service (acceptance date). However, if the designated receiving agency did not annotate the invoice with the date of receipt at the time of actual receipt, the date the proper invoice is received is the date placed on the invoice by the contractor, regardless of the acceptance date.[3]

The technicians were required to enter three dates from the invoice into the IAPS system: the actual invoice receipt date, the invoice preparation date, and the acceptance date. IAPS then automatically selected the later of the invoice receipt date and the acceptance date to calculate a payment due date.

Selection of the Actual Invoice Receipt Date. DFAS Dayton Network selected an incorrect actual invoice receipt date on 18 of the 33 invoices. The 5 Code of Federal Regulations (CFR) 1315.4 states:

- For invoices that contractors mail, the actual invoice receipt date is the date a proper invoice is actually received by the designated agency office. It further requires that the agency annotate the invoice with date of receipt at the time of receipt (date stamp).

- For invoices electronically transmitted, the invoice receipt date is the date a readable transmission is received by the designated agency office, or the next business day if received after normal working hours.

The Vendor Payment Desktop Guide states that the date stamp should clearly identify the designated receiving office. The IAPS Manual directs the technicians to enter the invoice preparation date in the invoice receipt date field in IAPS if there is no acceptable date stamp.

For example, if the contractor submitted an invoice dated December 1, 2005, and the designated receiving office properly annotated that they received the invoice

[3] For the remainder of this report, the term "Actual Invoice Receipt Date" will refer to the date that the designated Government agency physically receives the invoice. "Invoice Preparation Date" will refer to the date the contractor places on the invoice. "Acceptance Date" will refer to the date the designated agency receives the goods. "Proper Invoice Receipt Date" will refer to the date that is used to calculate the payment due date.

on December 15, 2005, the invoice receipt date entered in IAPS should be December 15, 2005. However, if the designated receiving office did not annotate when they received the invoice, the invoice receipt date entered in IAPS should be December 1, 2005.

For 6 of the 18 invoices with receipt date errors, DFAS Dayton Network entered an actual invoice receipt date that did not identify the receiving office, as required by the DFAS Vendor Pay Desktop Guide. If the receiving office is not identified, DFAS Dayton Network must use the invoice preparation date. For another three invoices, DFAS Dayton Network selected the date it received the invoice, but the contract required another Government agency to receive the invoice and that date should have been used. For the remaining nine invoices, DFAS Dayton Network used the invoice preparation date when the invoice was date stamped, or used the incorrect date stamp when another agency was the designated receiving official. An incorrect invoice receipt date could result in either an early payment to the contractor (and subsequent interest lost to the Government) or an underpayment of interest to the contractor.

The IAPS Guide and the Vendor Payment Desktop Guide were both accurate when discussing the invoice receipt date that the technicians should enter into IAPS. However, additional clarification could help in some places where the guidance was vague as to whether the contract should be reviewed to determine the designated receiving office. DFAS Limestone has developed a "Pert Data Sheet" in which employees enter, among other things, the designated receiving office, and where to easily find that information in the contract or contract modification. This practice would be an efficient, effective way for all IAPS technicians and certifying officers to help determine if the correct invoice receipt date was used, along with additional training for the technicians and the certifying officers.

Selection of the Acceptance Date. DFAS Dayton Network entered an incorrect acceptance date on 20 of the 33 sample invoices.[4] The Act and 5 CFR 1315.4 state that acceptance is the 7th day after the date on which the property is actually delivered or performance of the services is actually completed (constructive acceptance). However, if the agency has actually accepted the property or services before the 7th day, the actual acceptance date must substitute for the 7th day after the delivery date.

For example, if the contractor delivered the goods on March 1, 2006, the agency accepted the goods on March 15, 2006, and constructive acceptance occurred on March 8, 2006, then the constructive acceptance date would be used as the acceptance date. However, if the agency accepted the goods on March 3, 2006, (prior to the constructive acceptance), then the March 3, 2006, date would be used as the acceptance date.

DFAS Dayton Network personnel did not properly select the actual acceptance date on four invoices and instead selected either the constructive acceptance date, date of delivery, or invoice receipt date. For another three invoices, DFAS Dayton Network either did not properly select the constructive acceptance date

[4] Five of these invoices also had an incorrect actual invoice receipt date selected.

and, instead, incorrectly selected either the invoice preparation date or the date of delivery, or DFAS Dayton Network selected a date that was not found in supporting documentation.

The 5 CFR 1315.14 states that for construction contracts, interest will begin to accrue 15 days after receipt of a payment request by the designated agency office. However, for six invoices, DFAS Dayton Network entered an acceptance date later than the invoice receipt date, which would result in a potential underpayment of interest.

For seven invoices, which did not require proof of acceptance, DFAS Dayton Network also did not correctly enter the invoice receipt date as the acceptance date. The contracting officers for these invoices permitted the contractors to be paid from the invoices without obtaining acceptance from the Government. Therefore, the acceptance date should have been the invoice receipt date.

The IAPS Guide provides guidance on entering the correct acceptance date. The IAPS Guide states that the earlier of constructive or actual acceptance is to be used except for construction contracts and direct submission invoices. It further states that the technicians should enter the actual invoice receipt date as acceptance date for construction contracts. However, while the IAPS Guide states that acceptance is not constructed for direct submission invoices, it does not specifically state that the actual invoice receipt date should be entered as the acceptance date. In addition, the Vendor Payment Desktop Guide does not provide detailed guidance on entering the proper acceptance date. Additional policy and training for technicians and certifying officers will help ensure that the proper acceptance date is selected.

Selection of the Proper Invoice Receipt Date. DFAS Dayton Network did not select the invoice preparation date as the proper invoice receipt date as required by the Act in six sample invoices.[5] The Act states that when the designated Government agency does not date stamp the invoice, then the invoice preparation date becomes the proper invoice receipt date. For the six invoices where the invoice preparation date should have been used, DFAS Dayton Network used various other dates, such as an improper date stamp or the acceptance date.

This occurred because the DFAS Dayton Network and IAPS did not have adequate controls to ensure that the proper invoice receipt date was selected when calculating the payment due date. Specifically, IAPS is designed to select the later of the Actual Invoice Received field and the Acceptance field. The DFAS Dayton Network training guidance directs technicians to enter the invoice preparation date in the Invoice Receipt Date field when the invoice is not properly date stamped, but does not direct the technicians to also enter the invoice preparation date in the Acceptance field when the designated receiving agency does not date stamp the invoice. Therefore, if the acceptance date is later than the invoice preparation date, IAPS will incorrectly select the acceptance date as the proper invoice date, which could result in an underpayment of interest to the contractor.

[5] The six invoices also had either actual invoice receipt errors or acceptance date errors.

Additional guidance should be provided to DFAS Dayton Network technicians to ensure compliance with the Act provision (31 U.S.C. 3901(a)(4)(B)) that requires the proper invoice receipt date be the invoice preparation date when the designated Government agency does not date stamp the invoice. DFAS Dayton Network needs to instruct its technicians to enter the invoice preparation date in both the Actual Invoice Receipt field and the Acceptance Date field when there is no proper date stamp on the invoice.

Calculation of Improper Invoices. For 18 invoices, DFAS Dayton Network personnel returned an improper invoice outside of the 7-day period allowable by the Act. The DFAS Dayton Network did not adjust the payment due date for any of the 18 invoices.

The Act states:

> When an invoice is determined to be improper, the agency shall return the invoice. . . no later than 7 days after receipt… When an agency fails to make notification of an improper invoice within seven days. . . the number of days allowed for payment of the corrected proper invoice will be reduced by the number of days between the seventh day. . . and the day notification was transmitted to the vendor. Calculation of interest penalties, if any, will be based on an adjusted due date reflecting the reduced number of days allowable for payment.

For example, if an improper invoice was received on November 1, 2005, and returned to the contractor on November 15, 2005, DFAS Dayton Network personnel should reduce the payment due date by 8 days (15 days to process the invoice minus the 7 days allowable by the Act.) If DFAS Dayton Network personnel do not factor in improper payments in the due date, potentially the vendor will be underpaid interest due under the Act.

The Vendor Pay Desktop Guide states that improper invoices should be returned within 7 days, but does not state what DFAS Dayton Network technicians should do if they do not return the invoice within 7 days. The IAPS Guide states that if DFAS Dayton Network personnel do not return an invoice within 7 days, the payment due date is adjusted to compensate for the additional days once the correct invoice is returned. However, it does not provide guidance on how to adjust the due date in IAPS or how to determine if there was a previously submitted improper invoice.

Controls Over the Return of Improper Invoices. For 37 sample invoices, DFAS Dayton Network personnel had not accurately and consistently coded the improper invoices in EDM. The IAPS Guide states that DFAS Dayton Network return invoices containing improper information or missing information to the vendor by the most efficient method as required by the Act. DFAS Dayton Network personnel should ensure all deficiencies are annotated before returning the document. In addition, DFAS Dayton Network should maintain a log to identify the documents returned and the following information on returned invoices: invoice number, vendor name, contract number, reason for return, date received in the designated billing office, and date returned. The Vendor Payment Desktop Guide and IAPS Guide require a letter annotating the deficiencies be sent

to the contractor with the improper invoice, and include examples of the form letter.

However, DFAS Dayton Network personnel did not keep a log of this information. As a result, the only way to determine if an invoice was previously returned to the contractor was to review all documents in EDM for that particular contract. In addition, a lack of controls existed over the method to annotate and return improper invoices in EDM.

For example, DFAS Dayton Network personnel stated that they would return the invoice to the Government official if they received the invoice from the Government official. However, the DFAS Dayton Network returned the invoice to that official without tracking the number of days the Government official took to return the invoice to the contractor. The Act is clear that the Government must reduce the payment due date by the number of days over seven that it takes to return the improper invoice to the vendor. To comply with this requirement, DFAS Dayton Network must track the total number of days it takes to return the improper invoice to the vendor. However, DFAS Dayton Network personnel returned improper invoices to an inappropriate official, such as the buying activity, in 9 of the 37 improper invoices sampled and only tracked the number of days it took to return the improper invoice to the buying activity. DFAS Dayton Network personnel should have returned the improper invoice to the contractor instead as required by the Act.

Controls over coding improper invoices needed improvement. For example, DFAS Dayton Network personnel did not properly code all returned invoices as "RTV" in EDM. Instead, DFAS Dayton Network coded some as type invoice or notes ("IN," "IN_RR," or "LOG"). In 18 of the 37 improper invoices, DFAS Dayton Network personnel coded the improper invoices as all three of these types of documents. The lack of consistency increases the risk that DFAS Dayton Network personnel will not properly identify an improper invoice and will improperly calculate the due date.

DFAS Dayton Network personnel coded 4 of 37 invoices as "RTV," although the invoices appear to have been paid and never sent back to the contractor for correction. In addition, some of the "RTV" sample invoices were sent back to the designated Government office for payment instructions. The implementing guidance for the Act does not cite a lack of payment instruction as criteria for making an invoice improper.

Many of the hardcopy invoices that were returned only had typed wording on the face of the invoice that it was sent back. In some instances, DFAS Dayton Network personnel did not enter a date or reason why the invoice was returned. Without this information on hardcopy invoices, DFAS Dayton Network technicians will not be able to determine how to adjust the due date. The Vendor Pay Desktop Guide requires a form letter to be mailed to the contractor indicating the reason for return. DFAS Dayton Network personnel should ensure that these letters are sent and keep a record of the supporting documentation.

DFAS Limestone Process. DFAS Limestone personnel developed a process outside of IAPS to improve the controls over improper invoices which includes

maintaining a database. The database includes invoice receipt date (as opposed to the scanned date maintained in the EDM records) and returned date. A DFAS Limestone supervisor stated that they also prepare a letter for the contractor informing them of the reason for the return, which is date stamped, mailed to the contractor, and then scanned into EDM. The designated Government office is also carbon copied on the letter if the invoice originally came from the Government official. Limestone then performs a reconciliation of this database with invoices that have been paid and checks to see if the technicians have properly adjusted the due date for the improper invoices over 7 days. While we did not audit the entire Limestone process, we noted that they have developed an internal database that tracks all invoices that have been returned.

Effect of Noncompliance

For the 75 sample invoices reviewed, DFAS Dayton Network personnel did not use the proper payment information on 61 invoices. As a result, DFAS Dayton Network made 42 payments that did not comply with either the cash management or interest penalty requirements of the Act. The noncompliance resulted in a total of $91,672.94 in interest errors.

The interest errors resulted when DFAS Dayton Network personnel made an early payment or they overpaid or underpaid interest due to contractors. Specifically, the DFAS Dayton Network made 16 payments earlier than allowable by the Act, resulting in $18,759.54 in lost interest savings. For the remaining 26 payments reviewed, the DFAS Dayton Network personnel underpaid interest to the contractors totaling $72,159.78 (67 percent of the total interest due) and overpaid interest to the contractors totaling $753.62 (2 percent).[6]

As a result of the lack of adequate controls, there is a high risk that DFAS Columbus and Limestone will continue to significantly underpay and overpay interest to contractors as required by the Act as they take over the payments. Also, DFAS Columbus and Limestone may continue to violate the cash management requirement of the Act by paying invoices earlier than 7 days prior to the payment due date, which will results in interest lost to the Government.

Recommendations, Management Comments, and Audit Response

1. We recommend that the Director, Defense Finance and Accounting Service Denver update the Vendor Payment Desktop Guide and the Director, Defense Finance and Accounting Service Columbus update the Integrated Accounts Payable System Guide to include detailed guidance to ensure compliance with the Prompt Payment Act. Specifically:

[6] The judgmental percentages do not project to the population.

a. Provide specific instructions on how to determine the proper payment terms, including the payment due date (that is, standard 30-day date or date specified in the body of the contract), and how to select the proper Prompt Payment Indicator.

Management Comments. The Director, Corporate Reporting Standards and Compliance, DFAS Indianapolis, concurred with the recommendation and stated that the DFAS Columbus training group wrote an IAPS Student Guide in March 2006 that replaced the outdated IAPS training course previously taught by Science Application International Corporation. He stated that the Student Guide replaced the Vendor Payment Desktop Guide and will be used at all paying offices. Further, DFAS Indianapolis stated that the Student Guide provides details on how to determine the payment terms and how to select the proper prompt payment indicator. DFAS Columbus planned to rewrite the Student Guide to incorporate new IAPS Database Expansion and Restructure release changes. DFAS Columbus planned to ensure the updated guide is available to all paying offices that process IAPS payments.

Audit Response. Management's comments were partially responsive. The Student Guide provided instructions for selecting an invoice receipt date and determining the acceptance date. However, the IAPS system automatically calculates the payment due dates based on the dates entered in the system, and the instructions did not address how to adjust the IAPS calculated due date when needed. The Student Guide does not provide instructions for what documents to view to determine the proper payment terms or how to update the data entered in IAPS. The Student Guide provides a description of the prompt payment indicator codes, but it does not provide instructions for how to select the proper code. Therefore, we request that DFAS Indianapolis provide additional comments outlining actions that will ensure that the Student Guide provides adequate instructions for determining the proper payment terms and prompt payment indicator code so that Vendor Pay systems calculate the payment due date correctly.

b. Provide specific instructions on how to:

1. Code returned improper invoices as "returned to vendor."

Management Comments. The Director, Corporate Reporting Standards and Compliance, DFAS Indianapolis, concurred with the recommendation and stated that the Electronic Document Management and Wide Area Work Flow system maintain information on rejected invoices. However, he stated that if DFAS rejects an invoice it is not entered into IAPS. He also stated that DFAS instructs users to document the reason for rejecting contractor invoices by adding notes in EDM and Wide Area Work Flow. Further, he stated that a Standard Operating Procedure was developed and distributed in December 2006 for DFAS Columbus personnel. The Standard Operating Procedure provides guidance on entering reason codes for rejected invoices and it will be reviewed for incorporation into an updated Student Guide expected to be completed by May 31, 2007.

2. Determine if there was a previously submitted improper invoice.

Management Comments. The Director, Corporate Reporting Standards and Compliance, DFAS Indianapolis, concurred with the recommendation and expects that the new Student Guide will improve the processing of rejected improper invoices.

3. Adjust the payment due date for any days past the 7 days allowable to return the improper invoice.

Management Comments. The Director, Corporate Reporting Standards and Compliance, DFAS Indianapolis, concurred with the recommendation and stated that the current Student Guide provides specific instructions on adjusting the payment due date for the number of days past 7 used to return an improper invoice. He also stated that DFAS Columbus planned to rewrite the Student Guide to incorporate the IAPS Database Expansion and Restructure release changes and will ensure the updated guide is available to all paying offices that process IAPS payments.

Audit Response. Management's comments were partially responsive. The Student Guide provides an example for adjusting the payment due date for an improper invoice that is not returned within the 7-day allowable window. However, the IAPS system automatically calculates the payment due date based on the dates entered in the system. The Student Guide does not provide instructions for updating the dates in IAPS to ensure that the time frame for making the payment reflects the number of days past the 7 in which DFAS is allowed to return the improper invoice. Additionally, the Student Guide instructs technicians to return improper invoices to either the vendor or the DoD organization, as appropriate. The Prompt Payment Act states that improper invoices should be returned to the vendor and does not include any provisions to return improper invoices to the DoD organization. Therefore, we request that DFAS Indianapolis provide additional comments outlining actions that will ensure that the Student Guide provides adequate instructions for adjusting the payment due date for any days past 7 used to return the improper invoice. The comments should also included proposed actions to instruct IAPS technicians to only return improper invoices to the vendor.

c. Provide detailed instructions to only use the Prompt Payment Indicator code B for bank payment contracts.

Management Comments. The Director, Corporate Reporting Standards and Compliance, DFAS Indianapolis, concurred with the recommendation and stated that the current Student Guide instructs the paying offices that process IAPS transactions to use the Prompt Payment Indicator code B only for bank payment contracts. He also stated that DFAS Columbus will rewrite the Student Guide to incorporate the IAPS Database Expansion and Restructure release changes and will ensure the updated guide is available to all paying offices that process IAPS payments.

Audit Response. Management's comments were partially responsive. The Student Guide explains that Prompt Payment Indicator code B means that interest does not accrue until after 30 days. The Student Guide also provides examples of when the code is used. However, it does not specifically state that the code should only be used for bank payment contracts. Therefore, we request that DFAS Indianapolis provide additional comments outlining actions that will ensure that the Student Guide provides adequate instructions for technicians to enter Prompt Payment Indicator code B only for bank payment contracts.

2. We recommend that the Director, Defense Finance and Accounting Service Columbus provide additional training to the technicians to ensure the Prompt Payment Act and related policies and procedures are followed. Specifically, the Defense Finance and Accounting Service should provide training to the technicians and certifying officers related to:

a. Determining the proper payment terms, including the payment due date (that is, standard 30-day date or date specified in the body of the contract), and how to select the proper Prompt Payment Indicator.

b. Selecting proper invoice receipt and acceptance dates.

c. Returning invoices to the contractors by mailing a letter indicating the reason for returning an improper invoice and keeping a record of supporting documentation.

Management Comments. The Director, Corporate Reporting Standards and Compliance, DFAS Indianapolis, concurred with the recommendation and stated that the DFAS Columbus training group wrote an IAPS Student Guide in March 2006 to replace an outdated IAPS training course previously taught by Science Application International Corporation. He also stated that the Student Guide provides instructions on how to determine the proper payment terms, select the proper invoice receipt and acceptance dates, and return invoices. Further, he stated that classes are provided to all incoming personnel and personnel recommended for training by management. He added that DFAS Columbus will rewrite the Student Guide to incorporate the IAPS Database Expansion and Restructure release changes and will ensure the updated guide is available to all paying offices that process IAPS payments.

Audit Response. Management's comments were partially responsive. Although the Student Guide provides instructions for selecting the invoice receipt and acceptance dates, the Student Guide is silent on the documents to view to determine the proper payment terms. Therefore, we request that DFAS Indianapolis provide additional comments outlining actions on providing training to IAPS technicians and certifying officers related to determining the proper payment terms.

Appendix A. Scope and Methodology

We requested all invoices that were subject to the Act paid in IAPS from April 1, 2005, through March 31, 2006. We received a database from DFAS Denver that contained payments records with the contract number, invoice number, invoice received date, payment date, contractor name, and payment amount. DFAS Denver also provided data fields indicating whether they earned a discount or paid interest on the invoice. We then selected a judgmental sample of 75 payments for testing to ensure compliance with the Act. In selecting the sample, we selected high dollar invoices and ensured an even distribution of payments that appeared early, on time, and late based on the IAPS invoice receipt and payment dates. We also ensured that 30 invoices that DFAS Dayton Network included on the "RTV" spreadsheet of invoices returned to the buying activity or contractor as improper were included in our 75 sample invoices. According to DFAS these payments were made through the DFAS Dayton Network (including Orlando, Omaha, San Bernardino and Dayton). DFAS stated that there was no way to identify which location had processed the invoice.

For each sample payment, we reviewed scanned hard copy documents and IAPS data to determine whether the invoice was processed in accordance with the Act. Specifically, we verified that the actual invoice receipt date, acceptance date, payment terms (that is, the standard 30-day time period or other as specified by the contract and the Prompt Payment Indicator), proper invoice receipt date, and payment due date were correct. We then determined whether the invoices were paid early, on time, or late.

For those invoices that were paid later than the payment due date, we calculated the amount of interest due by multiplying the disbursement amount by the number of days late and the appropriate daily interest rate. We then compared our calculated interest and the actual interest paid to determine if DFAS Dayton Network overpaid, underpaid, or correctly paid the interest to the contractor. For the invoices that were paid earlier than 7 days prior to the payment due date without proper authority (that is, a cash management waiver), we calculated the amount of interest lost to the Government by multiplying the disbursement amount by the number of days early and the appropriate daily interest rate.

We performed this audit from March 2006 through October 2006 in accordance with generally accepted government auditing standards.

We relied on DFAS Denver to provide all payments that were subject to the Act within the specified time frame. We used a judgmental sample to determine if the information provided was valid or accurate. However, we did not verify that all payments were provided.

Use of Computer-Processed Data. We used computer-processed data obtained from the IAPS system to determine the universe of contractor invoices and to select a judgmental sample of invoices for testing. We did not perform a formal reliability assessment of the computer-processed data. However, we examined additional supporting documents from DFAS Dayton Network to verify the accuracy of the IAPS data provided and that the payment was made. We did not

rely on IAPS system controls to perform this audit. Our results were not negatively affected by not performing a formal reliability assessment of IAPS.

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

Prior Coverage

No prior coverage has been conducted on processing IAPS contractor payment in accordance with the Act during the last 5 years.

Appendix B. Report Distribution

Office of the Secretary of Defense

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

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 Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Reform
House Subcommittee on Government Efficiency and Financial Management, Committee on Government Reform
House Subcommittee on National Security, Emerging Threats, and International Relations, Committee on Government Reform
House Subcommittee on Technology, Information Policy, Intergovernmental Relations, and the Census, Committee on Government Reform

Defense Finance and Accounting Service Indianapolis Comments

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

DFAS-JJR/IN

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

SUBJECT: DFAS Management Comments to DoD IG draft report, Project No. D2006-D000FJ-0178.000, "Defense Finance and Accounting Service Dayton Network Compliance with the Prompt Payment Act", dated November 15, 2006

Attached are current management comments to the subject DoD IG draft report, "Defense Finance and Accounting Service Dayton Network Compliance with the Prompt Payment Act," dated November 15, 2006.

Questions your staff may have concerning these matters may be directed to Mr. Juan Camacho at 317-510-3463.

William E. Bergmeyer
Director, Corporate Reporting
Standards & Compliance

Attachment:
As stated

DFAS Comments on DoDIG Draft Report Number D2006-D000FJ-0178.000, "Defense Finance and Accounting Service Dayton Network Compliance with the Prompt Payment Act", dated November 15, 2006

Recommendation 1: We recommend that the Director, Defense Finance and Accounting Service Denver update the Desktop Vendor Guide and the Director, Defense Finance and Accounting Service Columbus update the Integrated Accounts Payable System Guide to include detailed guidance to ensure compliance with the Prompt Payment Act. Specifically:

Action Plan A: Provide specific instructions on how to determine the proper payment terms, including the payment due date (that is, standard 30-day date or date specified in the body of the contract), and how to select the proper Prompt Payment Indicator.

Management Comments: Concur - The Denver Integrated Accounts Payable System (IAPS) Office is responsible for the IAPS System Guide and DFAS Columbus is responsible for the Desktop Vendor Guide. In late 2005, the DFAS Columbus training group was tasked to write an IAPS Student Guide to replace an outdated IAPS training course taught by the previous training contractor Science Application International Corporation (SAIC). This was completed March 2006. The Student Guide will replace the current Desktop Vendor Guide. The Student Training Guide will be used procedurally at all paying offices as it is much more detailed than the Desktop Vendor Guide. This guide is very detailed on how to determine the proper payment terms, including the payment due date (that is, standard 30-day date or date specified in the body of the contract), and how to select the proper prompt payment indicator. The Student Guide will be rewritten due to the IAPS Database Expansion and Restructure (DEAR) release. The DEAR release estimated completion date (ECD) is May 2007. The DFAS Columbus training group is simultaneously working the DEAR release changes to IAPS. DFAS Columbus will ensure the updated guide is available to all paying offices processing IAPS payments.

Estimated Completion Date: August 01, 2007

Action Plan B: Provide specific instructions to:

1. Code returned improper invoices as "returned to vendor".

Management Comments: Concur - Electronic Document Management (EDM) is the system that maintains the official records for invoices received hard copy; Wide Area Work Flow (WAWF) is the record keeper for electronic invoices received. These

systems maintain the information on rejected invoices. If an invoice is rejected, it is not input into the IAPS. Users are instructed to document the reason for rejecting a contractor invoice by adding notes in EDM or WAWF, depending on how the invoice is received. A Standard Operating Procedure (SOP) was developed and distributed December 2006 for DFAS Columbus personnel. This SOP provides guidance on entering reason codes for rejected invoices. These reason codes will be reviewed for incorporation into the updated Student Guide expected to be completed by May 31, 2007.

Estimated Completion Date: August 01, 2007

Action Plan B: Provide specific instructions to:

2. Determine if there was previously submitted improper invoice.

Management Comments: Concur - The new Student Guide, to be completed after the IAPS DEAR release, will expand the processing of rejecting improper invoices.

Estimated Completion Date: August 01, 2007

Action Plan B: Provide specific instructions to:

3. Adjust the payment due date for any days past 7 used to return the improper invoice.

Management Comments: Concur - The current IAPS Student Guide gives specific instructions on adjusting the payment due date for any days past 7 used to return the improper invoice. The Student Guide will be rewritten due to the IAPS DEAR release. The DEAR release ECD is May 2007. The DFAS Columbus training group is simultaneously working the DEAR release changes to IAPS. DFAS Columbus will ensure the updated guide is available to all paying offices processing IAPS payments.

Estimated Completion Date: August 01, 2007

Action Plan C: Provide detailed instructions to only use the Prompt Payment Indicator code B for bank payment contracts.

Management Comments: Concur - The current IAPS Student Guide instructs those processing transactions in IAPS to only use the Prompt Payment Indicator code B for bank payment contracts. The Student Guide will be rewritten due to the DEAR release. The DEAR release ECD is May 2007. The DFAS Columbus training group is

simultaneously working the DEAR release changes to IAPS. DFAS Columbus will ensure the updated guide is available to all paying offices processing IAPS payments.

Estimated Completion Date: August 01, 2007

Recommendation 2: We recommend that the Director, Defense Finance and Accounting Service Columbus provide additional training to the technicians to ensure the Prompt Payment Act and related policies and procedures are followed. Specifically, the Defense Finance and Accounting Service should provide training to the technicians and certifying officers related to:

a. Determining the proper payment terms, including the payment due date (that is, standard 30-day date or date specified in the body of the contract), and how to select the proper Prompt Payment Indicator.
b. Selecting proper invoice receipt and acceptance dates.
c. Returning invoices to the contractors by mailing a letter indicating the reason for returning an improper invoice and keeping a record of supporting documentation.

Management Comments: Concur - The Columbus training group was tasked to write an IAPS Student Guide to replace an outdated IAPS training course taught by the previous training contractor SAIC. This was completed in March 2006. This Student Guide provides instructions on how to determine the proper payment terms, select the proper invoice receipt and acceptance dates, and return invoices. Classes are provided to all incoming personnel at the enduring sites, as well as personnel recommended for training by management at each site. The Student Guide will be rewritten due to the IAPS DEAR release. The DEAR release ECD is May 2007. The DFAS Columbus training group is simultaneously working the DEAR release changes to IAPS. DFAS Columbus will ensure the updated guide is available to all paying offices processing IAPS payments.

Estimated Completion Date: August 01, 2007

Team Members

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

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