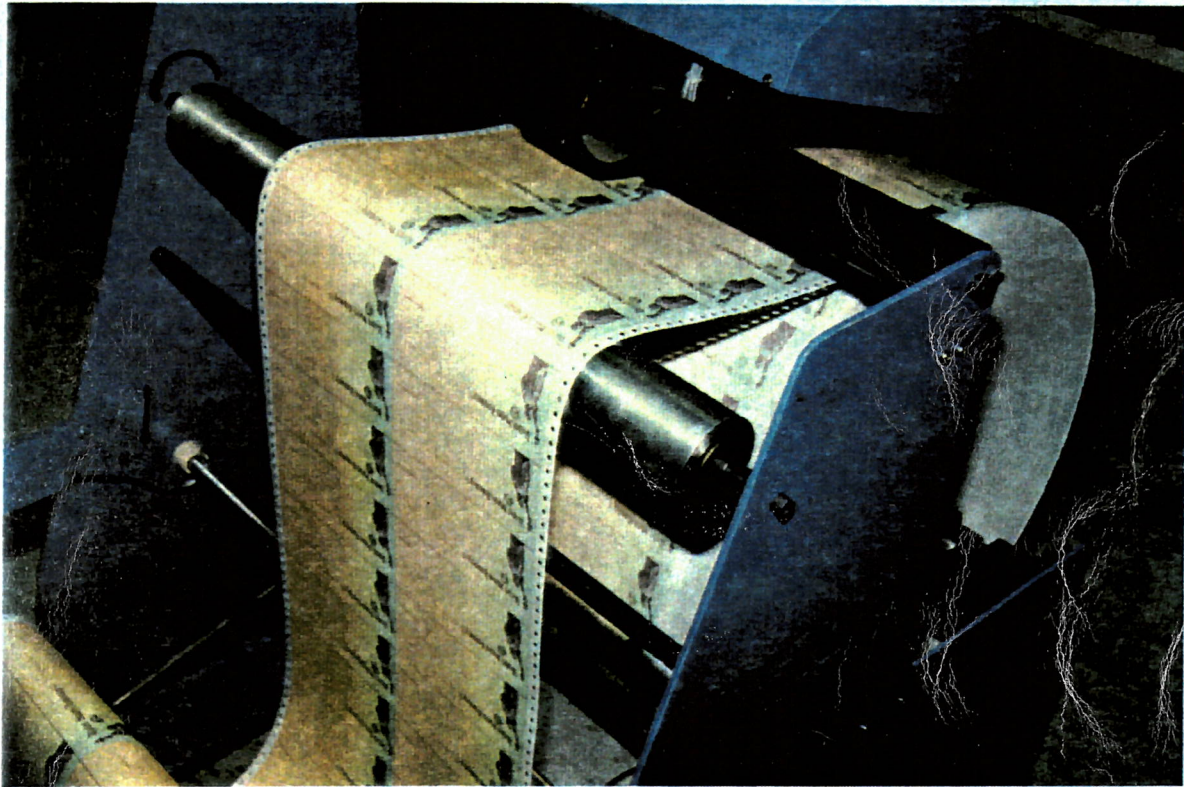


# Staff Report of Joint Review of Internal Controls At Department of Defense



By

**Mr. A. Ernest Fitzgerald**

Management Systems Deputy  
Department of the Air Force

And

**Mr. Charles H. Murphy**

Legislative Assistant  
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SEPTEMBER 1998

Staff Report

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September 1998

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21 September 1998

### MEMORANDUM FOR SENATOR GRASSLEY

SUBJECT: Joint Review

Enclosed is a copy of our "as of now" draft of the Report on the Joint Review of Internal Controls at DoD.

It has been more than a year since you and Mr. Hale chartered this review, and many expected closure in a few weeks. However, after reading our report and the associated GAO report and hearing the testimony of witnesses at the September 28 hearing, we believe you will agree with us that the problems are more serious, more wide-spread, and more deeply-rooted than any of us anticipated. It follows that opportunities for improving our stewardship are equally large if we follow through.

We are continuing to work on this draft. We ask that you allow us to brief you, preferably with Mr. Hale, at your earliest convenience.

*Charles Murphy*  
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OFFICE OF THE ASSISTANT SECRETARY

DEPARTMENT OF THE AIR FORCE  
WASHINGTON DC



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*A. E. Fitzgerald*  
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Management Systems Deputy

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Office of Senator Grassley

## REVIEW OF INTERNAL CONTROLS

In recent years, Senator Grassley has become increasingly concerned about the total breakdown of discipline in administrative and management controls at the Department of Defense (DOD). Senator Grassley's concerns grow out of a series of audit reports by the General Accounting Office (GAO) and the DOD Inspector General (IG). These reports consistently show that sloppy accounting procedures and ineffective or nonexistent internal controls leave DOD's financial accounts vulnerable to theft and abuse.

Senator Grassley is familiar with two DOD fraud cases that prove DOD's accounts are vulnerable to misuse: Lugas at Reese AFB, Texas; and McGill at Norfolk, VA. These cases caught his attention for two important reasons. They show: 1) How easy it is to tap into DOD's accounts and steal large sums of money - undetected; and 2) Fraudulent activity, if caught at all, is seemingly detected by chance and not as a result of effective internal controls.

The four cases mentioned in this report - Lugas, McGill, Krenik, and Miller - have been adjudicated in the courts. Lugas and McGill were sent to prison. Miller has just been sentenced to 12 years in prison, and Krenik pled guilty to making false claims and is still on probation.

### Pattern of Abuse - Other Cases

Justice Department (DOJ) statistics clearly indicate that the Lugas and McGill cases cited by Senator Grassley in speeches on the floor of the Senate are not isolated cases. Instead, they are part of a much broader pattern of theft and abuse. Moreover, controls are so weak that we are usually unable to tell from accounting records whether we received anything at all for outlays of the taxpayers' money or even that we knew specifically what we had ordered.

### 802 Other DOD Cases - 1997

In fiscal year 1997 alone, DOJ reviewed 802 cases involving financial crimes at DOD with 88 defendants pleading guilty; 66 imprisoned; and prosecution declined in 43 cases. Since 1992, DOJ has handled 2,490 similar DOD cases with 679 defendants pleading guilty, 451 persons imprisoned and 364 declinations.

Unfortunately, the DOJ statistics are just the tip of the iceberg. Only we don't know how big the DOD iceberg really is. It is very difficult to gauge the true dimensions of financial crimes, especially where controls are as weak as the ones we reviewed. Most criminologists believe that only a fraction of fraud and embezzlement cases are reported, and most are not detected.

For the private and public sectors together, the Federal Bureau of Investigation estimates that 15,700 workers were arrested for embezzlement in 1996 - up almost 25 per cent since 1993, according to an article in USA Today, January 13, 1998, entitled "Embezzlement Growth is Dramatic." According to this report, a recent survey of 2,600 certified fraud examiners revealed that U.S. businesses lose more than \$400 billion annually to fraud, nearly a third of that from embezzlement. This article indicates "there's been a dramatic increase in embezzlement across the board." **The main reason given for the increase is: "lax internal controls."**

Lax internal controls are the subject of our report.

### Joint Review

In July 1997, based on continuing concerns about the vulnerability of DOD accounts to theft, Senator Grassley launched an in-depth review of the case of the former Air Force employee, Mr. Mark J. Krenik; of the circumstances that allowed this fraud to move through the system undetected; and, if possible, to make a start on corrective action.

With the cooperation of the Secretary of the Air Force, it was agreed that the Krenik review would be a joint project. As part of the arrangement, the Management Systems Deputy for the Air Force was authorized by Assistant Secretary for Financial Management Robert Hale to participate. This was a joint project between Mr. Hale's office and the Judiciary Subcommittee on Administrative Oversight and the Courts. The Management Systems Deputy for the Air Force is Mr. A. Ernest Fitzgerald, co-author of this report.

### Purpose of Review

The joint review examined the following issues:

- What did Krenik do?
- How did he do it?
- Did he act alone, or did the Hughes STX Corporation or anyone else participate in the scheme?
- Are there other examples of fraud similar to Krenik's.
- Does DOD have new controls in place to prevent Krenik-style fraud in the future?
- What additional controls are needed?

### GAO Support

The GAO formed a special team to support the joint review. Its Accounting and Information Management Division and Office of Special Investigations (OSI) provided audit and investigative support. GAO will issue two reports as follows:



- 1) DOD Procurement Fraud: Embezzlement by Air Force Contracting Official;
- 2) Financial Management: Air Force needs to Improve Vendor Payment Systems and Controls

These reports are being issued separately and will be released at the time of the Subcommittee's hearing on September 28, 1998.

The first report - issued by OSI - will address the mechanics of Mr. Krenik's scheme and the involvement of the Hughes STX (Hughes Aircraft/General Motors now Raytheon STX) in submitting the least five fraudulent invoices for \$342,832.00 at Mr. Krenik's direction. Although the GAO concluded that the Hughes Corporation collaborated with Mr. Krenik in a scheme to defraud the government, the GAO attempted to lessen the wrong-doing by straying from the documentary evidence and relying almost exclusively on unsubstantiated assertions provided by company officials.

The second report attempts to establish the scope of Mr. Krenik's crimes and assesses control weaknesses in light of the new case involving Air Force Staff Sergeant (SSGT) Robert L. Miller, Jr., at the Defense Finance and Accounting Service Center in Dayton, Ohio.

#### Review of Internal Controls

Between June 1997 and July 1998, we conducted an independent review of internal controls at DOD.

#### Testing Controls

The purpose of this effort was to assess the effectiveness of internal controls today in a place where they were demonstrated to be weak or nonexistent in the past - Mr. Krenik's former place of employment. During Mr. Krenik's tenure, this organization was known as the 7th Communications Squadron. Today it is known as SAM, for Single Agency Manager for Pentagon Information Technology Services. SAM controls acquisition of computer equipment and services, audio-visual equipment, and other material - as in Mr. Krenik's day - for many organizations in the Pentagon, primarily for the Air Force at the time of our review.

We quickly saw that the criminal justice system was inadequate as a substitute for tight, on-going management controls focused on individual transactions and separation of duties. Clearly, the justice system - the courts, backed by investigators, auditors, and enforcement officers - are critical backstops. However, this system is analogous to a baseball back stop which is only one yard square. Most uncaught balls miss the backstop completely.

In our opinion, it would be unrealistic to expect otherwise. We need prevention, or at least powerful inhibitions, of financial misconduct at all levels of seriousness from criminal down to careless waste.

We also need visibility and accountability. Missteps, whether deliberate or simple mistakes, can be detected and corrective actions taken before the problems grow into monsters - if we know about them.

So, we set out to review the entire acquisition cycle in which the Krenik syndrome was embedded. We hoped to see:

1. Statements of what was needed and justification for those needs.
2. Responsive contracts let by independent purchasing organizations clearly defining purchases, citations of appropriation-linked funds from which the bill would be paid, and clear agreements between the buyer and the seller.
3. Documentation of delivery of goods and services specified in the contracts with certification of delivery by authorized persons in organizations independent of the buying organization.
4. Receipt of invoices (bills) from contractors, comparison of those invoices to contract requirements and to certification of receipts for goods and services. This matching should be done by an independent financial control group. If they find everything matches, this group should prepare a certification (voucher) that the bill should be paid. This is the accounts process and was a major focus of our review.
5. Payment of properly supported vouchers by another organizationally independent group. This is a treasury function and is accomplished by the Treasury Department for most Executive Branch agencies, but the DFAS does it for DOD.

#### No Books of Account

Ordinarily, a review of internal controls might be expected to include not only what we got for our money, but the disposition and status of what we bought. However, where tangible goods were added to inventories of supplies or equipment, one might also expect to find accounting records of these assets kept by organizations separate from those having physical custody. Unfortunately, we knew we would not find such arrangements, so we did not spend much time looking. We also knew that custodians of equipment were allowed to keep the item records, if any were kept, and that no dollar values were assigned to inventory. It is, therefore, not possible to tie these assets to the books of account, and that is why the books don't balance..

#### "Pay and Chase"

"Pay and chase" is Pentagonese for paying bills without receipts.

In today's climate of "streamlining" for streamlining's sake, organizational separation of duties for internal check is denounced without factual bases. For example, DFAS asserted that paying bills without first checking if money is owed ("pay and chase") would save money. There is no evidence of any such savings. In theory, we were supposed to save clerical time in accounts payable processing, but there is no evidence of real savings, and off-setting costs have been ignored. The actual result of paying bills without receipts has been chaotic operations, with much highly inefficient back-tracking and extra work which would be unnecessary if logical sequences of operations had been followed routinely.

The pay and chase concept confused even the DOD Comptroller. In June of 1995, he wrote in The Washington Post that the DOD was "... reversing a 25-year-old 'pay first account later' policy", and that for every supposedly "lost payment" and "phantom payments", the department had "a validated receipt with an independent confirmation that the government received the goods and services." Actually, so far as we can tell, DFAS' pay and chase policy was announced to the Air Force in October 1994. During the course of our review, we were told that the pay and chase "experiment" ended in October 1997 after the DOD General Counsel decided it was illegal. As a result of this decision, Secretary of Defense Cohen asked Congress in February 1998 for legal authority to pay bills without receipts - with no dollar limit. Fortunately, Secretary Cohen's misguided proposal was rejected. No one in Congress thought this was a very good idea. We don't know whether the practice has actually ended. It had not as of our visit to DFAS-Denver in March 1998.

#### Separation of Duties

Far from being costly red tape, organizational separation of duties has been viewed as an efficiency measure, especially for organizations large enough to afford specialization. For example, Eric Kohler wrote in his A Dictionary for Accountants: "Carefully designed internal checks often yield definite advantages and economies because of the relative efficiency of a specialized operation." After legitimate needs are established, buyers buy, receivers receive, store keepers store, inventory accountants account, accounts payable matchers match, and disbursers disburse. Each organizationally independent function takes care of business one transaction at a time, and they get good at it in well-run organizations. Only exceptions to the normal routine require special attention. As noted above, DOD does not routinely separate the duties of custody of assets and accounting for them. This should be an important consideration because of DOD's inability to keep track of assets and to prevent fraud. On this latter point, Mr. Kohler wrote:

"As long as accounting and custody are separated, fraud can be completely concealed only through collusion between employees responsible for each of these functions. Fraud by an employee in either function is virtually

certain to be discovered when quantities on hand (as reported by the custodial function) are verified with what the records show should be on hand (a product of the accounting function)."

### What We Did Not Do

There are seven related subject areas that we deliberately avoided due to time constraints. Those are summarized briefly below:

1. We did not examine the roles of account holders in the overall panoply of controls.
2. We did not focus on fraud involving collusion with contractors. Most typically, we have observed over the years that the taxpayers are milked by a government employee "taking care of the contractor" and the contractor taking care of the employee in another transaction. Because of weaknesses in overall controls and often misdirected management emphasis, the taxpayers are nearly defenseless here. With the exception of Mr. Krenik's Hughes caper, the breakdowns we focused on were what appeared to be one-party frauds, and we believed protections could be strengthened here right away.
3. We did not concentrate on "typewriter ribbons" and the like, as some critics of our review charge. Until now, such items have been stocked in dispersed stationery stores which issue supplies to the users who pay for them on a government-issued credit card with a budgetary ceiling. It is true that some of the payments we looked at were small according to Pentagon standards, but such examples were offered to us and were almost invariably partial payments to cover incremental deliveries on much larger contracts. We encountered only one example of a "progress payment", which is an advance payment secured by a work-in-process inventory to be delivered later. We did not follow this trail even though progress payment control is a huge problem. However, this is a separate process and should be addressed as a separate but a related problem.
4. We did not examine nor challenge seriously the need for purchased goods and services, despite some serious doubts about real need. This should be an on-going activity by a pro-active, cost-cutting budget function, an activity which we fear will have to await the coming and recognition of hard financial times.
5. We did not thoroughly review the contracting process. We tried in connection with the Krenik syndrome itself, but found it a blind alley. One of our first requests was for copies of the statements of work and delivery schedules for the two Hughes contracts on which Mr. Krenik committed fraud. One was missing altogether, and in the other work to be done was only vaguely described. "Deliverables" were examples only, things which might or might not be delivered at some unspecified future date. Any specific future deliveries of goods and services under the contract would be described ("definitized") by other parties under supplementary documents called

"delivery orders". The basic contract was essentially just a green light for others, such as Mr. Krenik, to spend money more or less as they wanted with or through the contractor. Under this set-up, Mr. Krenik and others like him, have control of the entire cycle from delivery order preparations to submission to DFAS for payment.

Individuals such as Mr. Krenik are either Contracting Officer Technical Representatives (COTRs) or Contracting Officer Representatives (CORs). They may create orders for more or less anything they want and certify the resulting bills for payment. Or, they can order nothing at all, or receive nothing at all, and certify that for payment as well, as Mr. Krenik did. We recognize this whole procedure needs re-vamping, but it was beyond our near-term ability to deal with.

We did look at some of the "small purchase" contracts (defined as up to \$100,000 but scheduled to rise to \$250,000!), but found definition usually lacking there, too.

The whole contracting area needs re-working.

6. We did not systematically question prices despite almost irresistible temptations to do so. This, also, needs on-going challenge and testing if we are to have any assurance that we are paying only what genuine needs should cost.

7. Except for our incomplete review of cash management, we did not dig into other accounts which should be connected to accounts payable. Reasons for this are illustrated by the following definition of accounts payable from Professor Ralph Estes' Dictionary of Accounting:

#### accounts payable

Amounts owed to others, often restricted to amounts due to suppliers. Accounts Payable is a *current liability* with a normal credit balance. The most common journal entries affecting the accounts occur when material is purchased:

#### Purchases for Materials

Inventory	xxx	
Accounts Payable		xxx
and when accounts are paid		
Accounts Payable	xxx	
Cash		xxx

As the definition shows, accounts payable should be examined in connection with inventories and cash. Services would normally be charged to work-in-process inventories, or to carefully controlled overhead accounts - neither of which exists here. Some of the items we examined cry out for formal inventory control tied to the books of

account. Computer and audio-visual equipment is a big part of what we're supposed to be buying in the area we examined. These are "pilferable" items much desired by individuals and businesses.

There is an excellent case in point. A former Drug Enforcement Administration official was sentenced to more than two years in prison on September 11, 1998, for using phony purchase orders to buy \$850,000.00 of audio-visual equipment and convert it to her own use.

The financial management community has largely brushed aside this problem.

This omission is facilitated by ignoring the traditional use of double-entry bookkeeping. Apparently, DOD is not alone in government in this regard. The following excerpt is from the testimony of Agriculture Department Inspector General Roger C. Viadero before the House Government and Reform and Oversight Committee on July 9, 1998.

"The depth of the Forest Service's accounting deficiencies is so extraordinary that even the most fundamental principles, like double-entry bookkeeping first set forth in writing by the Venetian Monk Luca Pacioli in 1494, are not always honored."

No wonder we can't "balance the books". Double-entry bookkeeping is the way assets have been accounted for and balanced against liabilities for at least 500 years. Furthermore, failure to post entries in the books correctly deprives the taxpayers of a key accounting control: Continuous reconciliation of accounts payable with cash and formally controlled inventories to help assure we received something of value for the money spent.

#### Searching for "Leaks and Holes"

We tested controls by tracking about 200 invoices generated by SAM through the entire cycle of transactions - from request to purchase; to the initial purchase order; to the contract; invoice; delivery verification; payment; and all the way through final reconciliation of checks issued versus checks processed by the U.S. Treasury.

The sample of 200 invoices was determined by DFAS and SAM and not by us. DOD provided the sample and we evaluated it.

In digging into the payment verification process behind each invoice, we searched for "leaks and holes" in the system. We probed for leakage by seeking answers to a set of questions on our abbreviated "checklist":

- Was the delivery of goods and services properly certified?
- Was each accounts payable file complete at the time of payment?

- Was the information in the accounts payable accurate?
- Did the invoice match with the contract?
- Was the contract valid and specific enough to later determine whether we got what we ordered.
- Was the amount paid the same as the amount authorized in the contract for the delivery of the goods and services specified in the contract?
- Was there any variance in remit addresses (address where check is sent)?
- Do issued checks match with checks processed by the U.S. Treasury?

#### Four-Phased Review

The review of internal controls governing the payment of SAM's invoices was conducted in four distinct phases.

In Phase 1, we began by conducting a cursory examination of about 200 invoices generated by SAM. The invoices examined ranged in dollar value from a low of about \$50.00 all the way up to \$50,000.00. In Phase 2, we narrowed the focus of the review - somewhat. Based on a very quick examination of accounts payable files provided by the DFAS, we selected about 50 invoices for closer scrutiny. We then subjected those transactions to an intense review for five days while at DFAS's Denver center.

All the information and documents obtained at the Denver center were subsequently combined with information obtained in follow up meetings and discussions with vendors and SAM customers, including a number of on-site inspections. The follow up work done in Phase 3 caused us to narrow our focus even further - to the 26 case studies listed at the end of the report. These cases highlight the most troublesome systemic problems that we uncovered during the course of our review.

The four phases of the joint review were as follows:

Phase 1: We conducted extensive interviews at SAM's Logistics and Acquisition Directorate, including a visit to the SAM warehouse in Arlington, VA, to assess the delivery verification process. We accomplished this task by examining selected requests for receiving reports assigned to SAM by DFAS. These pertained to the 200-invoice sample provided by DOD and SAM.

Phase 2: We visited the DFAS center in Denver, Colorado that processes SAM's invoices for payment. During a visit in March 1998, we examined about 50 accounts payable files for completeness and accuracy.

Phase 3: We linked the paperwork in selected accounts payable files with specific customers - mostly in the Washington, D.C. area. Once a customer was identified, we attempted to locate and inspect the equipment to verify that the goods and services were, in fact, delivered.



Phase 4: We compared the U.S. Treasury checks issued by DFAS with the checks processed by the Treasury Department to be sure that the amounts and addressees matched.

#### Phase 1 -- Delivery Verification by SAM

Vendors doing business with SAM submit their invoices directly to the DFAS center in Denver. Once those invoices are received and entered in the computerized Integrated Accounts Payable System - called IAPS, the system automatically generates a request for receiving report. These reports are then delivered to SAM in the Pentagon for research and certification. They usually arrive in batches of 50 to 100 every several weeks, although sometimes the interval between reports is longer.

A request for receiving report should include all the pertinent information on each invoice as follows: 1) contract number; 2) invoice number; 3) invoice date; 4) vendor; 5) amount, and 6) description of goods and services received. There is no provision in these reports for identifying the goods and services delivered. However, due to our review, DFAS issued a directive in March 1998 specifying that "valid receiving reports" must include that information.

Once these reports are received by SAM, they are assigned to a contracting officer's representatives (CORs or COTRs discussed earlier). In October 1997, SAM had 77 CORs. CORs are authorized to verify the receipt of goods and services, among other things. In addition to signing the reports, the COR is supposed to "certify" that the goods or services were "received and accepted" on a specific date. That date is supposed to be entered in a blank space provided for that purpose at the bottom of each report. The receipt date is very important because it is supposed to be used to compute interest penalties on late payments as required by the Prompt Payment Act - 31 U.S.C. 3901.

To evaluate SAM's verification procedures, we examined about 150 requests for receiving reports covering the period June through October 1997. Our examination uncovered a number of serious control weaknesses or "leaks and holes" in SAM's anti-fraud mechanisms. These are listed below.

#### --"No DB Match"

During the review of one batch of request for receiving reports, we discovered that about 50 percent fell into the "NO DB Match" category ("DB" stands for "database"). A "NO DB Match" occurs when SAM is unable to find any supporting documentation on record for an invoice. The contract number cited on the report and invoice is not listed in SAM's database.

In most cases, we think the "NO DB Match" situation is caused by a failure to update the database as new contracts are issued and old ones expire. However, a "NO DB Match" should be treated as a red warning flag. But it is not. It could be an indicator of a

fraudulent transaction and needs to be treated with greater respect and concern by SAM. Today, "NO DB Match" is considered routine and largely ignored as insignificant, perhaps for reasons which became clear when we visited Denver.

#### --Verbal Certifications

The certifications provided by SAM's CORs are rarely - if ever - based on first-hand, on-site inspections. The COR or COTR does not personally visit the customer to verify that the goods and services were actually delivered. There is no provision, either initially or on follow-up, by organizationally independent authorities to verify and check at each step of the acquisition process.

Under normal circumstances, certification is accomplished verbally - with telephone conversations - but absolutely no supporting documentation. For example, the COR will contact the customer - or vendor - by phone. The customer will say: "OK, I have it." The COR then certifies delivery, clearing the invoice for payment. Sometimes, this procedure might be adequate. However, we found a SAM COR certifying delivery of services that were, in fact, never delivered. A verbal certification process allowed this to happen.

#### --Inaccurate and Incomplete Reports

Of the requests for receiving reports examined in detail, most were found to be either incomplete or inaccurate. As we pointed out earlier, specification of what was ordered and received is usually not a concern at SAM. We found that only about 30 percent of the reports were actually complete - signed, dated, and certified, while 70 percent were incomplete - unsigned, uncertified, or "rubber stamped." For those that were "complete", many of the delivery dates provided were determined to be incorrect. We determined that they were mostly inaccurate by independently checking all pertinent documentation provided by customers and signed packing slips provided by vendors.

#### --"Rubber Stamping"

The most dangerous practice observed was the use of Lieutenant Colonel (LTC) Fran Barner's rubber stamp. We know that SAM's "rubber stamping" operation contributed to at least one duplicate payment.

LTC Barner is Chief of the Logistics Division that is responsible for researching the DFAS' request for receiving reports. Her rubber stamp was used on about one-fifth of one batch of reports we examined. We were told that the rubber stamp was kept in LTC Barner's desk drawer for emergency use only. When a COR was unable to obtain any useful information on an invoice - like a "NO DB Match" - then an assistant was authorized to get it from the drawer and "rubber stamp it." The rubber stamp is used

when no supporting documentation can be found. When all else fails, the CORs use of LTC Barner's rubber stamp was authorized. The logic of this procedure remains unexplained.

In sum, most of the reports, which are researched and cleared by SAM, are either incomplete or inaccurate, and, for the most part, are based on no knowledge about the goods and services delivered. Yet, despite all these obvious flaws, these reports play a crucial role in the decision to pay a bill.

At DFAS, SAM's request for receiving reports are placed in the accounts payable files and treated like genuine - certified - receiving reports - as proof of delivery. That they are not!

#### --No Separation of Duties

Organizational separation of duties is one of the most basic but effective anti-fraud control mechanisms. Under this principle, no single individual in the purchase and payment process is authorized to perform more than one function. For example, a person, who orders goods and services, is not authorized to verify receipt of the same goods and services. Similarly, a contracting officer should never be allowed to verify contract performance. Or a pay technician at DFAS should not be creating obligations and changing remit addresses - addresses to which checks are sent. Checks and balances are needed. But checks and balances appear to be lacking throughout SAM's and DFAS' verification process.

We found a SAM employee assigned to the National Military Command Center (NMCC), who has multiple responsibilities and authority very much the way Mr. Krenik did. He is allowed to operate freely with little or no oversight or supervision. Over time, we discovered that he had the following authority and responsibilities:

- He is a customer
- He develops requirements
- He prepares purchase orders
- He has steered contracts to favored vendors
- He issues orders to contracting officers at Bolling AFB
- He revises purchase orders to cover cost overruns and other errors
- He is a contracting officer technical representative
- He has ordered unauthorized equipment for favored customers
- He certifies contract performance by signing receiving reports
- He controls inventory

We have no reason to believe that this person is engaged in fraudulent activity, but if he were a dishonest person, it would be very easy for him to do it. With the controls in place today in SAM, for example, he could order highly pilferable audio-visual equipment and divert it for personal gain. Or, he could order non-existent services and

have the check sent to a co-conspirator. There is nothing to stop him from doing it - other than his individual personal integrity. The lack of controls in SAM - as evidenced by this example - creates a dangerous situation. It invites fraud. It led people like Mr. Krenik into temptation.

#### --Direct Deliveries

Many of the Standard Form 1449 contract documents we examined specified that deliveries be made to the SAM warehouse in Arlington, VA. Frequently, these instructions were ignored or changed and deliveries went directly to the customer. Some contracts, in fact, called for direct deliveries to the customer.

Having deliveries made to a centralized warehouse is a good idea for two reasons.

First, it allows an independent warehouse person, who has no personal interest in the goods, to verify receipt. A customer, by comparison, could have a personal stake in the delivery, and for that reason, could falsify receipts. An independent check by a warehouse person helps to short-circuit fraudulent activity by dishonest customers.

Second, a centralized warehouse facilitates inventory control. It is supposed to ensure that equipment is entered into property management systems at the time of delivery. This adds another layer of accountability, and if done accurately and completely, should help DOD balance the books - someday - if double entry bookkeeping ever becomes a reality.

In some instances, warehouse deliveries may be impractical - like a large furniture delivery for an office in the Pentagon. Those deliveries should be direct deliveries, but a warehouse person should be on hand to verify receipt of each item ordered and delivered.

#### Phase 2 -- Integrity of Accounts Payable Files

Between March 23 and 28, 1998, we visited the DFAS finance center in Denver, Colorado. During 5-day visit, we subjected about 50 accounts payable files to intense review. With several exceptions, these files pertained exclusively to invoices generated by SAM.

We expected to find a complete set of documents in each file since most of the transactions reviewed had been completed and paid. A small number were still being processed for payment. A complete accounts payable file should include the following documents:

- Purchase request - form 9
- Contract - form 1449
- Receiving report - DD-250 or a counter-signed 1449 (Blocks 32 to 42)

- Invoice - submitted to DFAS by vendor
- Payment voucher - form 1034

Not one of the files we examined appeared to be in order and ready - in our opinion - for payment.

The documents in each file should be internally consistent. They should harmonize with one another. The invoice should match with the contract. The receiving report should match with the invoice and contract. The payment voucher should accurately reflect key information on the invoice, receiving report, and contract. And the remit address on the voucher - the address to which the check is to be sent - should match with the remit address specified in the contract.

A complete accounts payable file can be a very effective anti-fraud device. The documents in the file should indicate that the goods and services ordered are legitimate; the money is owed; and the money is available to pay for them. The receiving report should indicate that the goods and services were, in fact, received and accepted. The voucher should indicate that the amount paid was correct, including any interest penalties that might be due.

Unfortunately, the near total absence of genuine receiving reports, extensive internal mismatches and inconsistencies, and the presence of fraudulent data totally undermine the effectiveness of this mechanism and leave these transactions vulnerable to fraud and abuse.

In addition, it is important to remember that good paperwork, by itself, is not a foolproof defense against fraud. All the documents in an accounts payable file might appear to be in order but could be completely and totally fraudulent - like in the Krenik case.

#### --Widespread Discrepancies

Not one of the files examined was 100 percent complete, correct, and ready for payment. Yet most had already been paid. All had minor deficiencies. Most had major discrepancies. None should have been paid.

#### ---Missing and Inaccurate Receipts

Not one file contained a genuine or valid receiving report. Most contained surrogate or dummy receiving reports, and in most cases where there were receipts, it was impossible to match the receipts with the invoice or contract. In three cases, the files contained no invoices, but the bills were paid using DD-250 receiving reports provided by the contractor. Receiving reports provided by the vendor do not constitute very credible or independent proof of delivery, and a receipt should never be treated as an invoice by the paying office.

In almost every case, the files contained a request for receiving report. These pieces of paper were viewed as legitimate receiving reports for purposes of disbursement of money at DFAS-Denver. Unfortunately, we found that 70 percent of the reports we examined were unsigned, undated, or uncertified. And, as noted above, most did not specify what was delivered. For those that were complete, we found that many of the dates for receipt and acceptance of goods and services were simply wrong. In addition to being inaccurate, these reports were misleading because they were taken as certification of delivery. These cannot qualify as certifications. They were based on either no knowledge whatsoever or second-hand knowledge obtained verbally from dubious sources - like the vendor. None was supported by documentation.

#### ---Extensive Internal Mismatches

In many cases, we were unable to match the invoice with the contract.

The most common problem was an inability to match the goods and services billed in the invoice with the goods and services authorized in the contract. Dollar amounts and quantities did not square. Some purchases were not authorized in the contract. Some were made far outside the scope of the contract. Performance periods didn't match. Goods and services were purchased before the contract took effect - or after it was terminated. We found illegal contracts that obligated funds before the appropriations were enacted. Another used expired appropriations. As already noted, this area needs much more scrutiny and evaluation by the department's financial managers.

#### ---Variance in Remit Addresses

We also found widespread variances in remit addresses. This is a dangerous situation. It leaves a gaping hole in DFAS's anti-fraud defenses.

The remit address is so important because this is where the money goes.

Some checks were sent to the correct remittance address - the one specified in blocks 17a or 17b of the contract document - standard form 1449. However, many others were sent to different addresses - usually the remittance address given on the invoice, which often differed from the address given in blocks 17a or 17b of the contract. And in some cases, we found company names and addresses on checks that did not match the names and remittance addresses on either the contract or the invoice. These were remit addresses of unknown origins. In at least one case, checks were mailed to a current but invalid address - a phantom company and address that do not exist - a fact confirmed by the Post Office, repeated phone calls and searches of the internet.

#### ---Remit Address: Vital Control Mechanism

We believe that the remit address is a critical control mechanism, because it's very near the end of the money trail. In the case of fraud, this is the last step before the criminals get their hands on the cash. It could be compared to a strategic military choke point. All the money has to pass through this gate before it reaches its final destination. If you succeed in blocking or controlling it, you may be able to prevent most fraud. If every check were directed to the correct address - a legitimate address, then the probability of fraud by single individuals would be much lower. We believe that fraudulent schemes - like the ones hatched by Lugas, McGill, Krenik, and Miller - would not have succeeded - if remit addresses were tightly controlled.

Our in-depth review of 50 transactions shows that there is absolutely no control over remit addresses, and we now understand why. A total of 286 technicians in the Denver center alone have authority to alter remittance addresses or to create new ones. And they do it with great regularity. A technician responsible for paying bills should never be allowed to monkey with remit addresses. In fact, DFAS should not be authorized to change remittance addresses.

By allowing pay technicians to alter remit addresses, DFAS is violating a number of fundamental principles, including separation of duties. This authority should reside in the contracting office and should only be authorized in documents signed by the vendor. Remit addresses should be recorded in a central registry and altered only under controlled circumstances at the vendor's request.

#### ---Falsified Information in IAPS

Key dates displayed on payment vouchers, which are used to compute interest penalties under the Prompt Payment Act, are consistently wrong. We uncovered proof that DFAS deliberately falsifies these dates to reduce or deny interest owed to the vendors.

#### ---Invoice Tampering

During our visit to the Denver center, we detected a number of unexplained irregularities pertaining to the control and date stamping of invoices. We believe that DFAS is consciously tampering with invoices. This tampering has the effect of circumventing the Prompt Payment Act and sets the stage for other fraud.

The date stamp on an invoice is very important because it is used - in combination with the date of delivery - to determine the amount of interest due - if any - under the Prompt Payment Act - 31 USC 3901.

#### ---No Invoice Control

First, we discovered that there is no accountable record of invoices received at the Denver center. It is impossible to obtain information on an invoice in the center until it is

entered in IAPS - and that can take a long time. If an invoice is "lost" - and that's a frequent event - there is no way of knowing whether the invoice was ever in the center, or if it was, when it first arrived.

Every invoice that is received at the center - and date stamped - should be simultaneously entered in a central database until paid. That would provide accountability where there is none. Both the authors and the GAO recommended this simple control tightening, but it was summarily rejected by DFAS-Denver management.

#### ---Excessive Invoice Receipt/Delivery Times

Second, we detected excessive time delays between the invoice date and the date stamp. In some cases, it was a matter of a few days or weeks. In many cases, it was months - typically 4 to 6 months. And in one case, it was nearly a year. The average time to pay a sample of 68 invoices was five months. At least two vendors told us that they had to "write off" several hundred thousand dollars of invoices that were never paid by DFAS.

#### ---Multiple Date Stamps

Third, we noticed that some invoices had multiple date stamps. Some had two date stamps. Others had as many as 3 different date stamps. Some had no date stamps. In cases where there was no date stamp, vendor fax dates were substituted. Some invoices are faxed back and forth between terminals until new receipt dates were established.

Each invoice should have just one date stamp, and that should coincide with the IAPS entry date and be used in conjunction with the receiving report date to establish any interest liability.

#### ---Duplicate Invoices

Fourth, we noticed that most of the invoices were not originals. They were duplicates or copies of the originals. What happened to the originals? Were they trashed or destroyed? DFAS claims they were "lost." Evidence presented to support the charges filed against Staff Sergeant Miller indicates that invoices at the Dayton center were trashed by the "bag full." This may be happening at the Denver center. One vendor told us that at least 30 per cent of the its invoices get lost in the Denver center.

#### ---Homemade Invoices

Fifth, we found about 10 invoices that appeared to be homemade. They had no company logos. They could have been manufactured at the center because every DFAS computer - and probably most vendor computers - have a built-in capability to generate invoices. Perhaps, they were re-manufactured by the vendor to replace originals that were "lost" or destroyed to hide date stamps? In some cases, the homemade invoices were

faxed to Denver to create new receipt dates. Faxing is a "work-around" for date stamping when the faxed invoice date is substituted for the "lost" invoice receipt date.

#### ---Voucher-Void-Revoucher Operation

We found evidence that DFAS deliberately falsifies information in IAPS to reduce or deny interest penalties owed to vendors. DFAS does it with the "voucher-void-revoucher" maneuver. It works like a laundry operation.

First, a voucher is created to pay a bill. Presumably this follows receipt of an invoice. The PPA [Prompt Payment Act] computation dates displayed on the voucher may be correct. Second, the voucher is voided or destroyed for bogus reasons. The original invoices is probably "lost" at this point - destroyed or trashed. An undetermined period of time is allowed to pass. When DFAS thinks the bill needs to be paid, perhaps due to pressure from the vendor, then a duplicate invoice is obtained or manufactured and revouchered. During revouchering, the invoice is given a new receipt date. This date is fabricated and totally false. DFAS uses a new copy of the invoice mailed or faxed by the vendor, or if necessary, it manufactures one. As an alternative, it may simply enter a later date without back-up. This process is described in detail in the Sun Microsystems case on pages 44-48.

#### ---Poisoned Control Environment

The "voucher-void-revoucher" maneuver is used to cheat the vendors and circumvent the law. The deliberate destruction of invoices and falsification of information in IAPS is a potentially serious crime. It may be a violation of 18 U.S.C.1001. SGT Miller was charged with violating this law. He has been accused of destroying invoices and falsifying information in IAPS.

More importantly, such illegal practices are not conducive to a healthy control environment, yet we believe they are officially sanctioned by DFAS management. They help to create an environment characterized by dishonesty and deception, and that kind of environment can become a breeding ground for potentially serious crimes - like larceny. It conveys the message that anything goes. Tampering with invoices and falsifying information in IAPS is just one small step away from outright theft and embezzlement. And that's exactly what happened at DFAS' Dayton, Ohio center in the case of Air Force Staff Sergeant Robert L. Miller, Jr. He just started manufacturing fraudulent invoices and vouchers with his own personal remit address, and the checks came rolling in.

#### --Unsigned Contracts

Every Standard Form 1449 contract document that we examined was signed by a government contracting officer, but none bore the signature of the "offeror/contractor" in block 30a. We think this omission raises questions about the validity of these contracts.

In such cases, the contractors are not legally bound to do anything. This situation is usually compounded by the absence of a definitive statement of work.

#### Phase 3 - On-site Inspections

Under most circumstances, a complete accounts payable file is a good defense against fraud. If effective separation of duties principles are practiced, an accounts payable file should indicate that the goods and services were, in fact, ordered and delivered, and the amount paid is correct with each step certified by an authorized person organizationally independent of others in the process. Odds are very high that the money is really owed. However, paperwork alone never provides a leak-proof defense. Paperwork can be defeated. With fraudulent receiving reports as in the Krenik case, a phony invoice can slip right through the net - especially if the accounts payable department is asleep at the switch - like at DFAS.

This condition makes random on-site inspections necessary - to verify delivery. Unfortunately, SAM does not conduct on-site verifications. This leaves another gaping hole in SAM's anti-fraud defenses.

As noted earlier, the verification process, especially after the fact, is made much more difficult by the absence of double-entry bookkeeping. Even where "accountable records" are kept of material on hand, they are spotty records kept by the same people who have physical custody of the material, and the records are not tied to the books of account. Indeed, since the "accountable records" are not required to include dollar values of material on hand, there is no meaningful link to financial records.

As a first step, the customer needs to be located, and we discovered that can be a real challenge by itself. We experienced considerable difficulty in finding customers. Once the customer was located, the goods and services which were delivered were checked. Model and serial numbers are essential for a successful on-site inspection. These numbers are usually listed in both service and purchase contracts but not always on invoices. In theory, the numbers in the inventory control system should match with the numbers on the equipment in place and the contract. Unfortunately, theory and practice are distinctly different at the Pentagon.

We conducted about 15 on-site inspections. Of those, only one checked out OK. The rest exposed serious discrepancies. We found :

- Furniture ordered and paid for but not delivered
- Cheaper Panasonic color TV monitors substituted for more expensive Sony units
- Highly pilferable TV monitor missing from inventory
- Mismatches between serial numbers listed in inventory control systems and equipment in place as compared to contracts
- Unknown ownership dates on lease-to-own copiers



- No proof of service delivery
- Time sheets for consulting services missing or non-existent
- Services billed and paid for but not delivered
- Unable to locate purchased computer equipment

#### Phase 4 - Check Reconciliations

We reviewed about 200 U.S. Treasury checks. These checks were actually issued by the DFAS center in Denver and processed by the Treasury Department.

When DFAS issues a "paper" check, all pertinent data on these payments is transmitted electronically to the Treasury Department on a weekly and monthly basis. Once the "paper" checks are cashed and processed by Federal Reserve Banks, a picture is taken of each one (front and back). The photographic image is then transferred to the Treasury Department's Check Payment Reconciliation Office in Hyattsville, MD for reconciliation.

The photographic image of each check is retained for at least six years.

Treasury matches the amounts on checks issued with the amounts on checks processed. Millions of checks have to be reconciled every year. Discrepancies are detected with great regularity. If the discrepancy cannot be resolved, it is referred to the Secret Service for investigation.

On April 16, 1998, the GAO reported \$4 billion in discrepancies between the checks issued by DFAS and the checks processed by Treasury. The main cause for the discrepancies is not known. Some could be caused by sloppy bookkeeping, but some could be the result of criminal activity - such as counterfeiting. In fiscal year 1997, the Treasury Department identified at least 20 DOD checks that had been altered or were counterfeit.

On each of the 200 checks examined by us, key pieces of information on the check itself were compared with the same information on the payment voucher (form 1043), including the date, voucher number, remit address (voucher only, not other records), and amount.

This was the only control area examined where no major discrepancies were found. We got a perfect match in dollar amounts and addresses. This finding should not be interpreted as meaning all is well with remit addresses. Here, we are saying that we found no discrepancies between addresses on vouchers and those appearing on the checks we examined. As we noted earlier, we uncovered widespread and dangerous mismatches between remit addresses specified in contracts and those appearing on vouchers and checks.

While no major discrepancies were discovered, we think there is a potential control problem that needs to be addressed. It concerns electronic payments.

#### Electronic Fund Transfers (EFTs)

A small proportion of the payments reviewed were Electronic Fund Transfers or EFT's. EFT's are not subjected to independent verification by the Treasury Department like "paper" checks. EFT's are assigned symbol serial numbers and are processed through the Federal Reserve Banks - just like a "paper" check, but there is no reconciliation process for EFT's by the Treasury Department.

With the computer capabilities available to the general public today, an electronic payment can be intercepted, altered or diverted just like a "paper" check, so EFT's need to be checked, too.

We are afraid that altered or counterfeit EFT's may fall through the cracks. Treasury says DOD is supposed to be checking EFT's, but DOD is not doing it. DOD says Treasury is doing it. This kind of dangerous mis-communication needs to be ironed out.

Each EFT payment should be subjected to the same reconciliation process as a "paper" check. And the responsibility for doing it belongs outside of DFAS and DOD.

#### Conclusions

##### --Air Force Promises - No More Krenik-Style Fraud

As we began the joint review one year ago, an Air Force liaison officer, Colonel Philip E. Ruter, presumably writing for the entire Air Force, gave Senator Grassley an ironclad assurance that corrective actions had been taken. Strangely, the Air Force Management Systems Deputy, who was the Air Force designated representative on the joint review, was not informed of this conclusion, and is still trying to determine who in the Air Force actually provided it.

The Air Force liaison officer's letter to Senator Grassley declared in no uncertain terms that a Krenik-style fraud could never happen again. This is what the Air Force said to Senator Grassley: **"The process has developed more internal controls to prevent this type of action from happening again."** The ironclad assurance was given in a memorandum on July 18, 1997.

At first, we were very skeptical about the validity of the Air Force's ironclad assurance, but, nevertheless, used it as our starting premise, and looked for evidence that effective controls were in place. However, as time passed and our review progressed, our mistrust gave way to total disbelief. We now believe it was false.

This belief is bolstered by specific findings of our joint review.

--The Krenik Case

Examination of the Krenik case, which triggered the joint review, is far from complete. However, we encountered so many information gaps and blind alleys that Senator Grassley asked for GAO help. Even with the GAO's broader skills and more abundant resources, a number of important holes in our understanding remain. Many unanswered questions remain.

To begin with, we still don't know what equipment Hughes was supposed to be maintaining under the contracts managed by Mr. Krenik.

Hughes STX contracted to deliver over \$50 million dollars worth of computer equipment and services under a FY 1986 multi-year contract and continued to support it up through CY 1996 under a series of costly maintenance contracts. There is no record that any of this equipment was ever delivered or placed in the inventory, though several Hughes STX "servers" were located in the Pentagon. Contracting officials at Bolling AFB told us that the contract was terminated in 1996 because: "We could not get a list or complete inventory of Hughes STX equipment to be maintained."

As noted earlier, contract definition is so bad as to give little or no information on what was ordered and what, if anything, was actually delivered. And, since DOD does not believe in double-entry bookkeeping or inventories controlled by the books of account, there are no known accounting records to show receipt or disposition of this stealthy, if not phantom, equipment.

We need to know what was bought and what happened to it. We need to know if this whole operation was fraudulent or was perhaps illegal for other reasons. We need to know why Hughes, which clearly cooperated with Mr. Krenik for a time in one of his frauds, was given immunity from prosecution without a proffer of what information or other help they would give in return. In fact, Hughes admitted making false claims.

In his successful plea for clemency, Mr. Krenik wrote that his defalcations were "so easy", and that he knew others were falsifying documents. There is no record and no admitted knowledge of why no one ever asked Mr. Krenik which other people were falsifying documents.

In this same vein, Mr. Krenik communicated with Senator Grassley that he had additional pertinent documents which he offered to the Air Force investigators and to the prosecuting U.S. Attorney. Mr. Krenik wrote that they were not interested. The prosecutor was not made available to staff for interview prior to the release of this report.

This is what Mr. Krenik communicated to Senator Grassley on February 2, 1998.

We quote:

"I have very extensive notes about all that was going on at the time. The U.S. Government, as represented by Mr. John J. Klein (Federal Prosecutor, Eastern District of Virginia) stated the Government had no need for my information. Nothing was offered to me (i.e., leniency) in exchange for my information. So why should I give this information away now? The Government told me they didn't want it."

We need to know why.

We need to know why working papers and reports of the Air Force Audit Agency (AFAA) were destroyed and at whose initiative.

In March 1993, the Air Force investigators asked the Air Force Audit Agency to conduct a comprehensive audit to determine the true scope of Mr. Krenik's financial crimes. Official Air Force records clearly indicate that the audit was conducted and, in fact, completed in December 1993. On February 10, 1998, we were informed that **"all the papers associated with the audit were destroyed."** The audit materials were destroyed during FY 1997 - possibly after we started asking questions. Under Air Force regulations and law, audit records involving suspected fraud and criminal activity must be retained or at least 6 years or at least until 1999.

We have conflicting stories on the source of the instruction to destroy these records. We need to know why there is no apparent interest in finding the missing records, reconstructing them, or even in resolving the evidentiary conflict.

We found a number of serious shortcomings in Air Force controls in organizations still dealing with Krenik syndrome matters. These short-comings need to be addressed.

We believe AFAA also found at least weaknesses in administrative controls and documented them in their papers. We believe that on at least one occasion, AFAA was blocked in an attempt to convey this fact in a letter to Senator Grassley. We need to know if AFAA was squelched, if so, who did it and why.

We need to understand the role of the Air Force General Counsel in the Krenik affair and in our joint review. We know they have played - and are playing - a central role, but we don't know what it is, and all attempts to get interviews with attorneys in the General Counsel's office have been rebuffed.

We have also been rebuffed in attempts to learn Mr. Krenik's work history. This kind of information helped to shed much light in the similar case of Air Force SSGT Robert Miller.

We need to know if there is any connection between Mr. Krenik's light sentence and the truncation of broader disclosures in the Krenik/Hughes case. The primary Hughes suspect was the project manager, Mr. Alan R. Jenkins, yet when the Air Force OSI and the Assistant U. S. Attorney wanted to find out if he was telling the truth, they asked that a lie detector test be given to him. The polygraph test was indeed conducted, but it was administered and paid for by Hughes (General Motors) in Michigan. When the results came back, they concluded that Mr. Jenkins was telling the truth. Based on this piece of information, the U. S. Attorney declined to prosecute the case. How could that happen?

#### --Miller Case

Sgt. Miller was employed by DFAS at its large Dayton, OH, finance operating location (OP LOC) between 1995-1997. With full access to the Integrated Accounts Payable System (IAPS), Sgt. Miller was able to create bogus obligations, contracts, and invoices which, in turn, generated fraudulent payments. In all, he generated almost \$1 million dollars in fraudulent U.S. Treasury checks according to charges against him. These payments went first to his mother, then his girlfriend, and eventually most of the money ended up on his pockets.

We believe that SSGT Miller was caught in the same way as Mr. Krenik - by chance and other causes. Internal controls were not a factor in the detection of crimes allegedly committed by either Mr. Krenik or SSGT Miller. Mr. Krenik's fraud was initially detected by an alert teller at the Maryland National Bank where he had stashed all the money. The teller became suspicious about one of his transactions and called the law. Based on all the evidence given to us, we believe that the person who blew the whistle on SSGT Miller was a concerned subordinate who had been sexually harassed by him. When her complaints were largely ignored, she turned against him. This person admitted engaging in fraudulent activity on SSGT Miller's orders and just waited for him to make a mistake, which he did. His routine error was then used as the pretext for reporting a fraudulent transaction to a supervisor and then to the Defense Criminal Investigative Service. In our opinion, no other explanation seems plausible. We saw too many other mistakes - big and small - that were either ignored or completely overlooked by DFAS. The person who finally blew the whistle on SSGT Miller probably had extensive prior knowledge of his fraudulent activities.

The timing of the Miller case was particularly damaging to the credibility of the AF liaison officer's July 18, 1998, claim about no more Krenik-style fraud. The Miller investigation was formally started on June 3, 1997, about six weeks before the Air Force's unfortunate letter. Furthermore, the underlying deficiencies which facilitated the Miller fraud had been widely known for years, and some of them had been reported to Air Force authorities and other investigative and audit agencies in the summer of 1996, about a year before the ironclad assurance. No effective corrective actions were taken. Worse,

the grave problems were covered up. The Air Force Management Systems Deputy had never heard of these grave failings, including management-condoned manufacturing of phony documents, until the facts emerged in the course of our joint review.

Beginning in September 1997, the joint review began to uncover gaping holes in SAM's and DFAS' anti-fraud defenses.

#### --Decorative Controls

A possible basis for the ironclad assurance that internal controls were working was the proliferation of new procedures and reorganizations. We found defensive mechanisms in place everywhere we went. However, for the most part, these were nothing but window dressing. They are mainly for show. At DFAS's Denver center, for example, the Director bragged about his 975-step control checklist. Unfortunately, based on hard evidence we gathered, it was ineffective. In fact, most people we talked to had never heard of it.

None of the control mechanisms we examined was fully operational. A control mechanism which is incomplete or partially effective is ineffective because it has "leaks and holes." Gaps in anti-fraud defenses are usually known to criminals and exploited by criminals. And, the gaps we saw were not just small openings. They were gaping holes big enough for a Mack truck to pass through. Even non-criminal lapses can be damaging to our taxpayers and to suppliers as well.

#### --Principal Findings

We believe that the internal controls in place today in SAM and DFAS are riddled with gaps. They leak like a sieve because of 11 major control deficiencies that we observed:

- #1 - Poorly defined contracts
- #2 - Bills paid without invoices
- #3 - Bills paid without receiving reports
- #4 - No follow up verification of delivery
- #5 - Irreconcilable mismatches between invoices and contracts
- #6 - No control over remittance addresses
- #7 - Inadequate separation of duties at every level
- #8 - Invoice tampering and falsified information in IAPS
- #9 - Inadequate accounting controls rooted in absence of double-entry bookkeeping and transaction-driven accounting.
- #10 - Improper management objectives and motivations.
- #11 - Control environment characterized by deception and dishonesty

#### --Glaring Deficiency - No Valid Receiving Reports

As recounted earlier, on June 10, 1995, DOD made another bold assertion that doesn't hold water. The DOD Comptroller, Mr. Hamre, claimed that there was a "validated receipt - DD-250" to back up every DOD payment. This statement is as untrue today as it was three years ago. As with the July 18, 1997, ironclad Air Force assurance of no more Krenik-style fraud, we have been unable to identify the origins of Secretary Hamre's misinformation. However, we are quite sure he could clarify the situation since he was subsequently promoted to Deputy Secretary of Defense.

The most glaring and persistent shortcoming we observed was the near total absence of valid receiving reports in the accounts payable files examined at the Denver center.

A receiving report is a valuable tool. It is not foolproof, but it constitutes an important starting point for delivery verification. It should provide accounts payable technicians with written certification that the goods and services billed on an invoice were, in fact, received, accepted, and matched what was ordered. In addition, receiving reports will be vital if we should ever decide to protect the public purse with double-entry bookkeeping and concomitant control inventories for equipment. However, receiving reports need to be spot checked with random, follow up on-site inspections. This is especially important in the absence of double-entry bookkeeping and formally controlled inventories.

In all the files we examined, and that's about 200, we found only 6 genuine receiving reports - DD-250 forms. The rest contained no official receiving reports. All 6 DD-250's that we did find were either invalid or incorrect. Three were provided by the vendor, which cannot possibly qualify as an independent proof of delivery. The other three were signed by an authorized government representatives but certified receipt of unauthorized services.

#### --Case Studies

The dangers associated with these 11 control deficiencies became crystal clear in the 26 case studies listed at the end of our report. These were culled from the invoice sample provided by DOD.

Each case pertains to an individual invoice that was paid by DFAS. Each one is an in-depth assessment of the documentation underlying an individual payment - in many cases validated by meetings with customers and on-site inspections. In some cases, information had to be verified in consultation with the vendor. Each one exposes major control weaknesses.

All pertinent documents, including the contents of Denver's accounts payable files, bearing on this case are located in the Subcommittee's files.

#### --Numerous Improper Payments Detected

We believe that our 26 case studies prove that internal controls in place today still leave DOD's financial resources vulnerable to fraud, theft, and abuse. They show that DFAS regularly pays bills that should not be paid at all and many more with inadequate justification. Erroneous, unauthorized, and fraudulent payments continue to slip right through the safety net - undetected.

Even if we were able to stamp-out fraud, the current system would still fall short of providing effective accountability to our shareholders, our citizens and taxpayers. The essential, primary purpose of the accounts payable process is assurances that we pay only for what was legitimately ordered and delivered. At present, the DOD financial community does not even display curiosity about what, if anything, was received or what happened to it.

Some might argue that erroneous payments are not good indicators of a control problem. We disagree. If underpayments or overpayments can slip through the net undetected, then there are serious quality control problems. Payments are not being checked for accuracy. And if there is a quality control problem, there is a control problem. And when there is a control problem, unauthorized, improper, and fraudulent payments can slip through the net undetected - as we repeatedly discovered during the joint review.

The 26 invoices included in our case reports generated payments totaling \$238,966.95. Everyone was improper. Some failings appeared to be minor. Others were major and very serious.

It is very important to understand that a small problem at DFAS can have a devastating downstream impact. DFAS pays 2 million bills every month. A \$50.00 mistake on half the payments becomes a \$600 million mistake in a year's time. A \$500.00 mistake on 10 percent of the monthly payments becomes a \$1.2 billion problem in a year's time.

We found improper payments of every size and description. For the 26 invoices in our sample, improper and erroneous payments totaled at least \$96,728.91 or 40% of the dollar total as follows:

#### --Underpayments: \$970.22

Most underpayments occurred when DFAS deliberately cheated vendors on interest penalties by tampering with invoices and falsifying information in IAPS. We don't have an exact estimate of the dollar value of all those discrepancies, but there were many such cases. A long and complicated computation is needed to arrive at a precise figure in each case.

We did compute the additional interest due on 7 selected payments. The total additional amount on those 7 payments is \$970.22. DFAS shortchanged the vendors involved and should pay them immediately - with additional interest that might be due - as follows:

- Cannon U.S.A., Inc. Case - pp 7-10 - \$148.76
- Government Micro Resources, Inc. Case pp 11-13 - \$107.80
- Domore/DO3 Case - (Combined with Invincible Office Furniture) - pp 20-23 - \$111.01
- Leightronix, Inc. Case - pp 24-25 - \$17.44
- Professional Products, Inc. Case - pp 39-41 - \$112.61
- Sun Microsystems, Inc. Case - pp 44-48 - \$440.18
- Washington Professional Systems Case - pp 54-56 - \$32.42

--Overpayments: \$854.10

Overpayments occurred when DFAS paid for goods and services that were not authorized in contracts:

- Canon USA, Inc. Case - pp 7-10 - \$2.10
- Government Technology Services, Inc. Case - pp 14-15 - \$816.00
- Xerox Corp. Case - pp 57-60 - \$36.00

These are minor amounts in Pentagon terms, but nevertheless represent a quality control problem as a minimum. DFAS should search out assignable causes of defective work, eliminate the causes, and disseminate lessons learned.

--Unauthorized Payments: \$71,403.98

Unauthorized payments occurred when DFAS paid for goods and services for which there was no contract authority. The vendors submitted bills for purchases made either before the contract was signed or took effect, or after it expired. There simply was no contract to cover the goods or services billed. We also found one illegal contract with Government Micro Resources, Inc. [pp 11-13]. It obligated \$55,797.36 before the appropriations were enacted. While we examined only one invoice for \$4,545.86 charged to the illegal contract, in all probability the entire amount has been or will be expended. This is a possible violation of the Anti-deficiency Act and other laws. Unauthorized payments were as follows:

- Canon USA, Inc. - \$243.69 [Case Index, pp 7-10]
- Government Micro Resources, Inc. - \$4,545.86 [Case Index, pp 11-13]
- I-Net Wang - \$25,991.54 [Case Index, pp 16-19]
- Openware Technologies, Inc. - \$13,049.27 [Case Index, pp 35-38]
- RGB Technology, Inc. - \$619.02 [Case Index, pp 42-43]

- Sun Microsystems, Inc. - \$26,322.60 [Case Index, pp 44-48]
- Xerox Corp. - \$632.00 [Case Index, pp 56-60]

--Duplicate Payment: \$636.95

We found one duplicate payment. The first time the bill was paid it was charged to the wrong contract. The second time it was paid it was charged to the correct contract. The vendor returned the money - \$625.58 - on July 30, 1998. This was the payment charged to the wrong contract. The duplicate payment follows:

- Liebert Corp. - \$636.95 [Case Index, pp 26-27]

This payment was one of those "supported" by LTC Barner's rubber stamp.

--Suspected Fraudulent Payments: \$21,603.66

We detected two possible fraudulent payments. The vendor, Sybase, submitted bills to DFAS for consulting services delivered to another private company, Synergy, using a bogus DOD contract number. These services were never delivered to DOD. The bills were paid by both Synergy and DFAS. Sybase returned some of the money to DFAS - \$19,462.72 - on May 22, 1998, after we raised the issue during our March 1998 visit to DFAS Denver, but the balance is still outstanding. The suspected fraudulent payments follow:

- Sybase, Inc. - \$21,603.66 [Cases Index, pp 49-53]

--Phantom Payments: \$1,260.00

DFAS sent at least 2 checks to a company that may not exist. The company's name is ALMCO. The company's address is in Costa Mesa, CA. DFAS assured us that it had "verified" this address - the address to which it sent the checks. On April 28, 1998, Senator Grassley addressed a letter to the company at the Costa Mesa address. Within a week, it was returned with this Post Office notation: "Return to Sender - Insufficient Address." The letter was undeliverable. Repeated searches of the Internet and phone directories and phone calls failed to confirm the existence of the company. This may be a phantom company. We don't know for sure. Our suspicions about this company were first raised when we examined the contract with the firm. It states: "This company does not have invoicing capabilities. Advance payments are authorized". Although AMLCO has no invoicing capability, we found invoices in the files. The questionable payments to ALMCO follow:

- ALMCO Industries - \$1,260.00 [Case Index, pp 1-4]

In addition to the improper payments listed above, we found at least three cases (No. 9, 10 and 13) where equipment was ordered and paid for but not delivered. We do



not have enough information to estimate the cost of those losses. We are still trying to determine whether the \$33,000.00 of computer equipment ordered and paid for (Case No. 15) was, in fact, delivered by Motorola. We have been trying to conduct an on-site inspection but so far have been unable to locate either the actual customer or equipment.

--Most Troublesome Observation:

--A Poisoned Control Environment

The most destructive, anti-control force that we observed at the operational level was invoice tampering and the deliberate falsification of information in IAPS at DFAS. This appears to be official fraud sponsored by DFAS against the business community. We believe that these illegal practices contributed directly to the more serious crimes committed by SSGT. Miller at the Dayton center.

Officially sanctioned invoice tampering and falsification of information has a particularly destructive effect on internal controls. It destroys the very fabric of internal controls. Documents suggest that these seemingly illegal practices were known to senior DFAS officials, including Mr. John Nabil, Director of the DFAS-Denver Center, but never reported to the proper authorities as required by law.

The Dayton operating location was under the control of the Denver Center when SSGT Miller was moved there from Castle AFB, California, which was also controlled by Denver. Though already under investigation for "losing" a large sum of cash entrusted to him as a "pay agent" at Castle, SSGT Miller was placed in a position at Dayton far above his rank. A much more senior civilian [GS-12] - Mr. Chuck Tyler, who occupied that position, was summarily removed to make room for SSGT Miller. SSGT Miller was "forced" into Mr. Tyler's position on October 19, 1995. Exactly one week later - October 26, 1995, the report on the investigation on the missing checks at Castle was issued. It recommends that SSGT Miller not be trusted with money. Again, he should have been removed from Vendor Pay at Dayton on the spot. But that did not happen. Why?

We believe SSGT Miller was hand-picked for the job by senior DFAS officials. His mission was to "fix" the problem. The invoice backlog and interest payments were far too high. His job was to get them down, and DFAS management apparently didn't care how he did it. Just get them down! Those were the orders which, according to witnesses statements, were passed through SSGT Miller to the technicians.

We believe that DFAS management knew exactly what SSGT Miller was doing and signaled approval by their actions and inactions. SSGT Miller, witnesses said, was destroying invoices by the bag full and falsifying information in IAPS to circumvent the law - the Prompt Payment Act. In fact, SSGT Miller's fraudulent activities were repeatedly reported to Air Force and DFAS authorities beginning in July 1996, but these

warnings were ignored completely or downgraded to nothing by all concerned. By tolerating these seemingly illegal practices, senior DFAS officials are helping to create a control environment that has been characterized by fraud and deceit.

We found evidence that some of the same illegal procedures are being practiced at the Denver center today. [See Sun Microsystems Case, pp 44-48]

A control environment characterized by deceit and dishonesty can become a breeding ground for more serious crimes - like embezzlement and larceny. Deliberately destroying invoices and falsifying information is just one small step away from larceny. In SSGT Miller's case, he made the transition with great ease. He simply entered IAPS; created bogus contracts; obligations, and invoices, and then generated fraudulent checks.

To a large extent, we believe that internal controls are a "state of mind".

The recent fraud case uncovered by the Director of Internal Audit of Virginia's Department of Transportation (VDOT), Mr. Alex Sabo, underscores the importance of "state of mind". In February 1997, substantial cost growth on the troubled FasToll System on the Dulles Toll Road was brought to the attention of senior VDOT officials, including Mr. Sabo. Instead of looking at cost growth as a funding problem and asking the Legislature for more money - as DOD would have done - VDOT considered uncontrolled cost growth on the project as cause for alarm. Questions were raised. What is causing the uncontrolled cost escalation? Independent inspection reports were checked. One question led to another and ultimately to the arrest of a crooked engineer who oversaw the project, Mr. Charles L. Williams, Jr. On December 2, 1997, he admitted in a Fairfax Court to embezzling \$336,000.00 in state money by submitting phony bills.

If the prevailing attitude is characterized by deceit, dishonesty, then even good controls can and will fail. This is the worst kind of control weakness. The casual acceptance of "a steady state of fraud" by top management amounts to abandonment of our stewardship responsibilities.

--Bottom Line

If the new controls are so effective - as promised by the Air Force, then why are so many improper payments slipping right through the control net - undetected? If the new controls are really working like they are designed to work, why was it so easy for us to find so many improper payments in such a small sample?

--No Effective Controls

We believe that the 26 case studies show that controls in place today are no more leak-proof than they were in Mr. Krenik's heyday. They can be easily penetrated and defeated.

### --Quick Fix

We fear that effective, comprehensive protections for the taxpayers' money will not occur until there is a dramatic change in attitudes toward good stewardship. However, there are a number of fixes to the accounts payable process as such which can be made now. These will produce immediate improvement and pave the way for broader protections later.

1. Write better contracts. For a contract to be anything beyond an excuse to give a contractor money, it must, as a minimum, define the goods and services sufficiently for a third party to determine later on if we got what we bought. The accounts payable master file in the accounts payable organization should be opened when the contract is approved by both parties. The contract should be date-stamped when received by the accounts payable organization and immediately entered into the electronic data base if one exists.
2. Prepare meaningful receiving reports. These should be approved by a person organizationally independent of the contracting organization who is authorized to receive goods or services on behalf of the government. A copy of the receiving report should be added to the accounts payable master file, which should already contain a copy of the contract. As soon as it is received, the receiving report should be date-stamped, and that date and the date of actual receipt should be entered into the electronic data base at that time.
3. Record invoice receipts promptly. Vendor invoices should be date-stamped when received, then immediately entered into the electronic data base. If steps 1 and 2 have been done correctly, matching of all entries on the three records - contract, receiving report, and invoice - can proceed immediately. A properly set-up electronic system should then be able to match all entries, including the dreaded "long line of accounting" automatically, kicking out only those items which do not match. Even without an electronic system, document matching will be much more orderly than at present, and vouchers authorizing payments should be more timely.
4. Don't allow improperly controlled changes. At present, many hundreds of people at DFAS are authorized to make changes in the IAPS data base, and the GAO reported that any hacker skilled in the art could break into the system. As we have seen, changes in records have been uncontrolled and in some instances deliberately manipulated. By and large, proper receiving reports were missing from DFAS-Denver records, but when they are re-instituted, they should not be subject to change by accounts payable

unilaterally. Improper changing or replacement of invoices or vouchers has been the principal means of defrauding vendors, and has facilitated some frauds against the government. "Remit to" addresses, destinations for payment, may be changed willy-nilly.

An easy quick fix, one which could be put in force right now, is to gain control of the process for changing remittance address. The remittance address is the address to which U.S. Treasury checks are sent.

Today, DFAS has unlimited authority to change remit addresses and does it with alarming regularity. The paying office - DFAS - should never have authority to alter remit addresses. That authority should be restricted to an organizationally independent contracting office. All remit addresses should be listed in a central registry. The addresses listed in the registry should be derived exclusively from the addresses specified in blocks 17a or 17b of the standard contract document - Form 1449. Those addresses should only be altered under controlled circumstances. The only way to change a remit address should be with a contract modification signed by the vendor.

We believe that one-party fraudulent schemes - like those hatched by Lugas, McGill, Miller - and one of those by Krenik - would not have succeeded if remit addresses had been tightly controlled. The GAO agrees.

Some other quick, straight-forward "fixes" are also in the offing. Both we and the GAO made numerous recommendations in the course of our review, and the operating managers have already agreed to put some of them in place. The new DFAS guidance on receiving reports - issued in March 1998 - is a prime example of constructive measures taken in response to the joint review. We intend to follow-up with other needed corrective actions. The GAO, for example, has agreed to work with us in the future in developing a standardized control checklist that can be used and understood at the working level.

Past and present-day experiences show that we should accept nothing less than solid demonstration that the taxpayers' interest are protected.

### DFAS "Budget Dust" or Mushroom Cloud?

Some may criticize our report because it focuses on improper payments involving relatively small sums of money. The invoices we examined ranged in size from a low of \$50.00 up to a high of \$50,000.00. This is chicken feed by DOD standards -- called "budget dust" in Pentagonese. But chicken feed at DFAS can turn into big money in a hurry. When chicken feed is multiplied by the 2 million invoices DFAS processes each month, pretty soon you are talking about real money. The small \$50.00 or \$500.00 problems uncovered in our sample easily become a \$1 billion problem in a year.

The improper payments that surfaced in our 26 case studies certainly constitute just a tiny slice of DFAS' \$22.2 billion in disbursements per month. That so many

improper payments were uncovered with such ease in such a small sample suggests, however, that the DOD-wide problem could be of staggering proportions. Certainly, we can offer our shareholders - taxpayers and citizens - no assurance that these DOD expenditures are under control.

Of the 50 accounts payable files we examined in depth, we detected improper payments in at least 26 cases or 50 percent of our sample. All 26 cases involved serious problems. But some were much more serious than others. We identified at least 10 cases or 20 percent of our sample that fell into the dangerous category. These are bills that DFAS should not have paid at all. They totaled \$96,728.91 or 40% of the dollar value of the 26 invoices we examined in detail. Assuming this is a representative slice and, for example, just 10% of DFAS payments fall into the dangerous category, then DFAS could easily be making \$25 billion in unauthorized or fraudulent payments every year.

A former Director of DFAS, Mr. Charles Coffee, admitted publicly in February 1996, that his agency makes \$1 million in "mistakes" every day. That equates to about \$20 million in "mistakes" per month or \$240 million a year. If DFAS is willing to admit to \$1 million of mistakes every day, then we think it is safe to assume that the figure is much higher.

In Mr. Coffee's mind, that's just a "half-percent error rate" and nothing to worry about. For him, that's apparently "budget dust." Given DFAS's size, Mr. Coffee appears to think such a small error rate is okay. Management appears to accept a "steady state of fraud" as the cost of doing business at DFAS.

DFAS loses more tax money in one day than the average citizen earns in a lifetime of hard work, and for reasons that defy understanding, DFAS thinks that should be acceptable to the average American worker.

We feel that the attitude toward the peoples' money exemplified by Mr. Coffee's remarks is totally irresponsible and unacceptable. It's intolerable.

If Mr. Coffee wants to behave in such a careless way with his own money, well, that's his business. But as Director of DFAS, he was entrusted with the peoples' money. He had a responsibility to account for every penny spent. We should strive to make every payment exact to the penny - no more or no less than owed. "Error rates" of one million dollars a day are completely unacceptable. Such error rates - and every shred of evidence we have seen - indicate that internal controls need to be tightened. And any person in DFAS who does not care enough to try to plug the leaks should be removed from office.

#### Desired Goal: Zero Mistakes

Mr. Coffee's attitude is not an inspiration to excellence. It encourages sloppy payment procedures and more mistakes. With that kind of attitude at the top, internal controls can never be tightened.

DFAS should have a goal of no mistakes. We know that mistakes will happen. But, when mistakes do happen, they need to be evaluated and prompt corrective action taken. And lessons learned from mistakes should be widely disseminated, not obscured, mischaracterized, or covered-up completely as in the past.

We plan to complete our review of the whole panoply of needed controls and to push for corrective actions and supplementary controls. The GAO has promised to help with this effort, and present indications are that support within DOD, at least in the Air Force, will broaden.

A glimmer of hope in the Air Force is the rescue of three of the former Air Force employees who got in trouble for being on the right side of wrong - doing in DFAS after being transferred to that agency. After these three were exiled to lesser positions and generally abused by DFAS management, Brig General Dennis Samic, Comptroller of the Air Force Materiel Command, re-hired them and assigned them to do meaningful work. General Samic said he re-hired them not just to rescue them, but because they were good help and he needed them.

This is a break with tradition. If not an isolated occurrence, it could be a beginning for setting the Pentagon's rewards and punishment system right-side up. Traditionally, people who help with or cover-up officially-tolerated (or encouraged) wrong-doing prosper while those who don't fall on hard times.

The taxpayers' employees must be free to voice their concerns without fear of adverse consequences. Fresh air and sunshine are the best disinfectants, and we need more of them. For the peoples' business, the First Amendment is the best management control ever devised and no other controls will work well without it.

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## ALMCO INDUSTRIES

We reviewed one invoice from this company - No. 7532. In examining this invoice, we detected several major problems as follows:

- Manufactured invoices
- Vendor has no invoicing capability
- Advance payments authorized
- No receiving report
- Falsified information in IAPS
- Invalid remit address
- A phantom company?

### Invoice

This invoice is dated June 23, 1997 and covers the delivery of 12 static drip pans (75"X36") at \$105.00 each for a grand total of \$1,260.00. The invoice states that all 12 drip pans were shipped on June 23, 1997.

The invoice itself bears no company logo and may have been manufactured by DFAS technicians at the Denver center. It is date stamped June 25, 1997 - just two days beyond the invoice date. It is most unusual for an invoice to be date stamped so quickly at the Denver center.

### Receiving Report

The accounts payable file at Denver contained no proof of delivery. There was no receipt or receiving report. In an attempt to verify delivery of the goods, Senator Grassley directed a letter to the purchasing office on April 28, 1998. To date, there has been no response.

### Contract

The contract was signed on June 12, 1997. It bears the signature of the government contracting office but has no vendor signature. It calls for the delivery of 12 static drip pans to be manufactured by ALMCO at a cost of \$105.00 each or a grand total of \$1,260.00. These items were to be delivered by July 6, 1997.

### First Payment

Despite the apparent absence of either an invoice or receipt, a partial payment of \$945.00 was made on September 26, 1997. Denver withheld \$315.00 - the equivalent of 2 drip pans - allegedly because a "bill had not been received." Why was DFAS making payment if no bill had been presented. The reason for the partial payment is a mystery.

## Variance in Remit Addresses

The remittance address - the address to which the check must be sent - is specified in block 17A of the contract document. That address was as follows: ALMCO Industries, 1422 SO. Gleneagle Road/P.O. Box 10948, Arizona City, AZ 85223. The first check was sent to this address.

### Invalid Address

About a month after the check was mailed - October 29, 1997, Denver attempted to follow up on the incomplete order. Denver notified the company at its Arizona City address that the delivery was incomplete and to "reinvoice" when complete. However, this notice was "undeliverable." It apparently sat in an Arizona post office for at least five months or until March 23, 1998, when it was returned to Denver with this notation "Moved, Left No Address."

We were told that the check for \$945.00 was returned to Denver on March 25, 1998 "due to a wrong address." It too was "undeliverable."

### Contract Modification

#### --New Address Established

On February 13, 1998, a contract modification was issued. It appears to have had two purposes: 1) Provide correct vendor address; and 2) establish new and inappropriate payment procedures.

This document officially changed the contractor's address to: ALMCO Industries, 629 Terminal Way, Costa Mesa, CA 92627.

#### --No "Invoicing" Capability

This document also authorized "advanced payments" to ALMCO. The document states: This "company does not have invoicing capabilities." The contract modification authorized payments without invoices.

ALMCO's lack of an invoicing capability appears to be an unprofessional business practice. How could a company doing business with the government have no capability to generate invoices? And if it lacked an invoicing capability, why would an invoice appear in Denver's accounts payable file?



### Second Payment

Consistent with the instructions provided in the contract modification, a second check was issued to ALMCO on April 3, 1998 in the amount of \$315.00. The check was sent to the new address in Costa Mesa.

The voucher indicates this was "ADV-PAY #1" to ALMCO. This payment was made without an invoice or receiving report or any proof whatsoever that the missing drip pans had, in fact, been delivered.

The first check for \$945.00 was re-sent to ALMCO's new Costa Mesa address on or about April 1, 1998.

The invoice has now been paid in full.

### Unresolved Issues

Evidence in the accounts payable file seems to indicate that technicians in the Denver center are manufacturing invoices and falsifying information in IAPS.

#### --Manufactured Invoices

The contract document states that ALMCO has no invoicing capability, yet the file contains an invoice from the company. How did it get there? Where did it come from?

The ALMCO invoice is unusual in appearance. It has no company logo and looks like it was homemade. The file also contained an IAPS document that had the word "dummy voucher" written on it. When asked about the word "dummy voucher," DFAS replied by saying that was "bad terminology." In reply, DFAS stated: "What should be actually referenced is the dummy invoice number because of advance pay. An invoice is not required on an advance pay but the IAPS system requires an invoice number so technicians used ADV PAY." DFAS' explanation is a source of concern. DFAS is saying a bill cannot be paid without an invoice number. Since there was no invoice and therefore no invoice number, one had to be created.

#### --Fictitious Dates for Manufactured Invoices

The particulars of the fictitious ALMCO invoice, created by technicians in the Denver center, are displayed on the payment voucher No. D800075336 dated April 3, 1998. The invoice date is March 30, 1998. The invoice was date stamped at the center on the same day - March 30, 1998 - unparalleled speed for DFAS/Denver. The goods were actually delivered on January 7, 1998. This invoice does not exist. All three dates are fictitious. There is nothing in the file to support them.

The phony dates displayed on the second voucher for the ALMCO invoice were created as if the first voucher for this invoice did not exist.

The original voucher for this invoice - No. D700104251 - was dated September 26, 1997. It indicates that the invoice date was June 23, 1997 - not March 30, 1998. The date stamp on the invoice was June 25, 1997 - not March 30, 1998. And the delivery date was September 11, 1997 - as compared to January 7, 1998. Both delivery dates are probably wrong. Since there is no receiving report in the file, the real delivery date is unknown.

It's also possible that all dates associated with this transaction are fictitious.

#### --Phantom Company?

Repeated attempts to contact and/or locate ALMCO were unsuccessful.

On April 28, 1998, Senator Grassley directed a letter to ALMCO at the new Costa Mesa address - an address that DFAS says it had recently "verified." Unfortunately, within about a week, the post office returned Senator Grassley's letter with this notation: "Return to sender; Insufficient address." It too was undeliverable.

Repeated searches of the Internet and phone directories in California and Arizona and numerous phone calls have failed to confirm the existence of this company.

Is ALMCO a phantom company?

### BTG, Inc.

We reviewed several invoices from this company but focused on just one - invoice No. 9608150. In reviewing this transaction, we detected several problems as follows:

- Bill took 2.5 years to pay
- Company has other unpaid bills totaling \$32,438.92 dating back to February 1996
- Phony invoice receipt date used to reduce interest penalty on old bill

### Invoice

The invoice is dated November 27, 1995. It covers the delivery of 5 TPFOT-2 converters at \$508.20 each. The total amount billed is \$2,541.00. The invoice is date stamped August 29, 1997. That means it took 21 months or nearly two years to reach the Denver center.

### Receiving Report

The accounts payable file at the Denver did not contain a valid receiving report. However, the file does contain a document that could be used as a receiving report. This is a request for receiving report dated April 9, 1998. It certifies that the goods were actually delivered on November 27, 1995. This date is consistent with a packing slip provided by the vendor.

### Invoice/Contract Match

The contract was dated June 22, 1995. It was signed by the contracting officer but not the vendor. It authorized the purchase of 5 TPFOT-2 converters for \$2,541.00 to be delivered by July 27, 1995.

The items billed in the invoice appear to match up with the items authorized for purchase by the contract.

### Circumvention of the PPA

This invoice was finally paid on May 8, 1998 - almost 2.5 years after it was first submitted. The payment included \$107.70 of interest.

The interest penalty due in this particular case was determined by the official invoice receipt date - August 27, 1997 or 21 months after it was presumably mailed. It is very difficult to believe that it took so long for the invoice to reach Denver.

The discovery of two other unpaid BTG invoices, totaling \$32,438.92, dating back to February 26, 1996, raise questions about the integrity of the DFAS date stamp.

### Remit Address

The contract provides a specific remit address in Richmond, VA. The check was sent to that address.

### CANON U.S.A., Inc..

We examined 21 Cannon invoices but focused on two - No.348022DEF145 and No. LR111406. In examining these invoices, we uncovered several problems as follows:

- Multiple date stamps on invoice
- No receiving reports
- Unauthorized services and payments
- Circumvention of PPA
- Falsification of information in IAPS
- Variance in remit addresses
- Impossible to match invoice with GSA copier rate structure without vendor assistance
- Special GSA pricing options and discounts not identified in contract

#### First Invoice - No. 348022DEF145

This invoice is dated March 28, 1997 and covers the delivery of a Canon model NP 6230 copier machine - serial No. NGM04901 - along with a supply of toner and a staple cartridge. It also includes a "trade-in charge back" discount for an older machine. The bill totaled \$6,721.48.

The invoice itself appears to be an original, but it bears at least two date stamps as follows: April 7, 1997 and August 20, 1997.

#### Receiving Report

The accounts payable file at Denver did not contain a receiving report for this invoice. However, a request for receiving report researched by SAM certified that the goods were "received and accepted" on March 21, 1997. Canon provided a signed receipt for this machine (Serial number NGM 04901, Model 6230) that confirms delivery and acceptance on March 21, 1997.

#### Invoice/Contract Mismatch

The contract is dated March 10, 1997 and bears the signature of the government contracting officer but no vendor signature. It covers the delivery of a Canon copier model 6230; trade-in on model 6650 plus warranty purchase; and allowance for monthly service charge for July through September. The award totaled \$7,007.38

The invoice matches up with the contract - with several minor discrepancies. A trade-in discount of \$539.02 was given on the invoice, but the value of the trade-in was not specified in the contract. Instead of paying the amount billed - \$6,721.48, only \$6,719.38 was due. DFAS overpaid \$2.10 for the toner.

The \$288.00 difference between the award amount and the invoice is the monthly service charge not billed on the invoice.

#### Circumvention of PPA

The second date stamp - August 20, 1997 - appears to be entirely fictitious, yet this is the date in IAPS used to compute interest under the PPA. Since the bill was paid on September 8, 1997, no interest penalty was considered due and none was paid - even though it took about 175 days to pay the bill.

First, there is the date stamp of April 7, 1998. That date is consistent with the March 28th invoice date and normal mail delivery and internal DFAS distribution times. Second, Canon sends multiple copies of each invoice to the Denver center every 30 days until payment is made. What happened to the invoices mailed in April, May, June, and July? Were they "lost" as DFAS suggests? And third, IAPS generated a request for receiving report for this invoice on August 4, 1997. These facts clearly indicate that this invoice was in the Denver center long before the "official" receipt date of August 20, 1997.

#### Pattern of Late Payments

Late or delinquent payments on Canon invoices is an old problem, and it persists today. In a meeting with officials in Canon's accounting department on May 1, 1998, we were told that Canon had 1,100 "open" invoices at Denver. Of those, 300 were classified as "overdue," including 99 that were more than 90 days late. Canon reported that it has had to "write off" invoices valued at \$133,000.00 that had been presented to DFAS/Denver in the past but never paid.

Assuming that the date stamp of April 7, 1997 and delivery date of March 21, 1997 are accurate, then an interest penalty of \$148.76 is still due and should have been paid to Canon.

#### Variance in Remit Addresses

Block 17a of the contract document provides the company's official address to which the payments are to be sent. This is the remit address. It is in Arlington, VA. The invoice, however, provides a different remit address in Baltimore, MD, and this is the address to which the check was sent. In this particular case, we don't think this variation is a problem, but it demonstrates an important control weakness. When technicians have widespread authority to change remit addresses - as in DFAS today, the potential for fraudulent payments is very high. The authority to change a remit address should be a closely guarded control. It's the last line of defense against fraud.

#### Second Invoice -- No. LR111406

This invoice, dated May 16, 1997, covered a service maintenance agreement for a Canon copier model NP4050 - serial no. NDV02610 - during the period August 1, 1996 through April 30, 1997 and meter usage for August 1996. The monthly meter allowance is 7,000 copies. Since only 3,208 were made, there was no additional charge for copies. The bill totaled \$1,096.56.

The invoice in the accounts payable file at Denver was not an original. It carries this notation: "This certifies this invoice to be a true copy of the original and has not been paid." This invoice bears just one date stamp - August 19, 1997.

#### Receiving Report

The accounts payable file in Denver contained no receipt for this invoice.

The request for receiving report in the file provides no service certification date. Despite the absence of this information, IAPS indicates that the service was actually delivered on August 19, 1997 - the same day the invoice was received and date stamped at the center. This appears to be another phony date. This date is particularly difficult to comprehend, because the invoice covers meter usage in August 1996 and routine monthly maintenance through April 1997. If the services were indeed provided, then they would have been delivered effective the last day of August 1996 and April 1997.

#### Invoice/Contract Mismatch

The contract is dated October 4, 1996. It bears the signature of the government contracting officer but no vendor signature. It covers maintenance on 8 Canon copiers for the period October 1, 1996 through September 30, 1997. The total award amount was \$12,440.40. The monthly charges and equipment serial numbers on the invoice match up with those authorized by the contract. However, there is a significant invoice/contract mismatch. The effective date of the contract is October 1, 1996, but the invoice bills for services rendered in August and September 1996. Payments for service during those two months - valued at \$243.69 - are simply not authorized. Those were unauthorized payments.

#### Circumvention of PPA

The date stamp on the invoice - August 19, 1997 - appears to be fictitious, yet this is the date used to compute interest under the PPA.

Since the bill was paid on September 8, 1997, no interest penalty was considered due or paid - even though it took 116 days to pay the bill. We believe the August 19th date is a phony date for several reasons. First, IAPS generated a request for receiving report for this invoice on August 4, 1997. This fact alone means that the invoice was in the Denver center and in the IAPS system in early August and probably long before that.

Second, Canon sends Denver multiple copies of each invoice every 30 days. Since this is a copy, we can assume that the original and subsequent copies were "lost" or trashed in the center.

#### General Contractual Problems

We noticed two problems that spanned all Canon invoices examined.

First, there is the problem of meter charges not authorized by contract. Of the contracts we examined, none authorized funds to cover charges for excess copies over the monthly meter allowance. Yet invoices regularly bill for excess copies over the allowance. This may explain why DFAS has occasionally told Canon that a bill "can't be paid. . . . There's just no money to pay the bill." This omission creates an over-obligation.

Second, the rate structure for copiers supplied to the government is extremely complex. The contracts, which we examined, are covered by a "blanket" GSA contract for all copy equipment leased and purchased by the government. We obtained a copy of the GSA contract document and attempted to match a Canon invoice with the information presented in the GSA document. It was impossible to do it successfully. We found the rate for the model number in the invoice, but each model number had different pricing options. Without a conversion table for serial numbers, which is not included, it is impossible to relate a Canon invoice to the GSA rate schedule. In addition, there are special discounts in effect that are not included in the GSA document. Technicians in the DFAS payment office and the contract office at Bolling cannot interpret copier pricing data without consulting with the vendor.

All special rates should be specified and funded in contract documents.

#### Variance in Remit Addresses

The contract provides a remit address in Arlington, VA. The check was sent to a different remit address in Baltimore, MD given in the invoice.

### GOVERNMENT MICRO RESOURCES, INC.

We reviewed five invoices from this company but focused on 2 - No. 57796 and No. 001196. In examining these invoices, we uncovered several problems as follows:

- Invoices fail to identify period of service
- Invalid and inaccurate receiving report
- Falsified information in IAPS
- Illegal contract

#### Invoice No. 57796

This invoice, which is dated February 10, 1997, covers on-site maintenance for a long list of computer software and related equipment - presumably for the month of January. However, the period of service covered by the invoice is not specified. It merely states: "period of performance, 1/1/97 - 9/30/97." That's the entire contract period. The total billed is \$4,255.20. Since the total value of the award was \$38,296.80 for 9 months, \$4,255.20 is the correct amount for one month, but which month?

#### Receiving Report

The accounts payable file at Denver did not contain a valid receiving report. However, it did contain a document that could have qualified as a receiving report - were it applicable to this invoice. The document - Standard Form 1449 - was signed by an authorized government representative - Kay Wegener. This person indicated that certain, unidentified items "for April 97" were received, inspected and accepted. The signature is dated May 5, 1997. Unfortunately, the reference to "April 97" indicates this certification probably applied to another invoice.

The accounts payable file for this invoice also contains a request for receiving report that indicates that the services were received and accepted on February 5, 1997. This certification was also given by Key Wegener. Since this was a monthly service contract, the services covered by the invoice should have been delivered - effective the last day of the month. In this case, that may have been January 31st.

#### Invoice/Contract Match

The contract is dated January 2, 1997. It is signed by the contracting officer but not the vendor. It covers software and equipment maintenance from January 1, 1997 through September

30, 1997 on a long list of equipment. The total award amount was \$38,296.80 or \$4,255.20 per month for 9 months.

The invoice appears to match the contract.

#### Circumvention of the Prompt Payment Act

The invoice is dated February 10, 1997 and date stamped on February 13, 1997. A 3-day invoice mail delivery and receipt period is excellent for Denver. Unfortunately, it took 155 days to pay this bill. A check was finally issued on August 12, 1997 and included an interest penalty of just \$6.38. The interest penalty paid is incorrect. A much larger sum is actually due.

Denver computed the interest due on this invoice by using a fictitious date - July 5, 1997. Denver claims that is the date when the services were actually delivered. That date is the driver behind this particular interest penalty. Unfortunately, there is absolutely nothing in the file to support the use of that date. It was invented to cheat the vendor. It was simply pulled out of thin air.

Assuming that the invoice receipt date of February 13th and the service delivery date of January 31 are, in fact, correct, then the vendor should have received an interest penalty of \$114.18. This is an underpayment of \$107.80 that must be paid to the vendor.

#### Invoice No. 001196

This invoice, which is dated February 28, 1998, covers hardware and software maintenance for a long list of computer equipment. The total amount billed is \$4,545.86. The period of service is not identified. However, since this is a monthly service contract, the invoice probably covers services delivered during the month of February.

There is no detectable date stamp on the invoice, but information in IAPS suggests that the invoice was not received until March 19, 1998 - nearly 3 weeks after being mailed.

#### Receiving Report

The accounts payable file at Denver did contain several conflicting documents that might qualify as a receiving reports - if they could be matched with the invoice. It contained a Standard Form 1449. It states that unspecified goods or services were received and accepted. Patricia Blakey's signature - the authorized government representative - is dated March 2, 1998.



However, another notation on the same document indicates that the form also covered "2nd QTR Payment - Jan - Mar 98." A second 1449 in the file, dated April 5, 1998 and also signed by Ms. Blakey, covered the "3rd Qtr Payment - Apr, May, and June." These certifications could apply to another invoice, since the bill under consideration was a monthly bill.

The accounts payable file also contained a request for receiving report - also signed by Patricia Blakey. The document indicates that the services were received and accepted on March 2, 1998. Yet the April 5th date - noted on one of the 1449's - was entered into IAPS and used as the PPA driver. Since the bill was paid on April 28, 1998, no interest penalty was paid. Both the invoice receipt date and service delivery date are suspect.

#### Illegal Contract.

The contract covered computer software and hardware maintenance for the period October 1, 1997 through September 30, 1998. The contract was signed by a contracting officer but not the vendor. The total award amount was \$55,797.36, but a subsequent modification lowered the figure to \$54,550.32 or \$4,545.86 a month.

This contract obligated \$55,797.36 in fiscal year 1998 appropriations on September 4, 1997. However, fiscal year 1998 appropriations were not enacted and available until October 8, 1997. So these funds were obligated prior to their availability. This is an illegal contract. It may violate several statutes, including the Anti-Deficiency Act - 31 U.S.C. 1341, which prohibits obligations without appropriations, and 31 U.S.C. 1502, which says that obligations may only be incurred during the period of availability for the funds used. There were no appropriations available when this contract was signed.

#### Remit Addresses

The contract for invoice No. 57796 provided a specific remit address in Washington, D.C. The check was sent to that address. The contract for invoice No. 001196 specified a remit address in Chantilly, VA. The invoice, by comparison, provided a remit address in Washington, D.C. that is identical to the one used on the check for invoice No. 57796. The check was sent to that address.

### GOVERNMENT TECHNOLOGY SERVICES, INC.

We reviewed at least 4 invoices from this company but focused on just one invoice - No. 217579701. In examining that transaction, we uncovered several problems as follows:

- Invalid receiving report
- Impossible to match invoice with contract
- Possible overpayment
- Falsification of information in IAPS
- Variances in remit addresses

#### Invoice

This invoice is dated March 4, 1997. It covers computer support services for a 4-month period - October 1996 through January 1997. The amount billed is \$1,224.00 or \$306.00 per month.

The invoice is date stamped July 31, 1997. That suggests it took nearly five months to reach the Denver center.

#### Receiving Report

The accounts payable file at Denver contained several documents that might qualify as a receiving report, but none appear to be valid.

Ms. Earlene Caper, an authorized government representative signed a form 1449, but it is undated and makes a vague reference to "monthly payment" and is not linked to a specific invoice.

A certification stamp was placed on the invoice itself. It is also signed by Ms. Earlene Caper. It states: "I certify the services and/or items for Oct96-Jan97 have been received." Her signature is dated July 23, 1997. This date is difficult to comprehend since this is a monthly service contract. The service for the month of October, for example, should have been delivered effective October 31st - Not July 23, 1997.

The accounts payable file also contained a request for receiving report. It is signed but undated and uncertified.

#### Invoice/Contract Mismatch

The contract was dated December 11, 1996 but had an effective date of October 1, 1996. It was signed by the contracting officer but not the vendor. It covered maintenance service on three "4/75" computer systems. Each unit to be serviced is identified by a serial number. The period of service is October 1, 1996 through September 30, 1997. The total award was \$3,672.00 or \$306.00 per month and \$102.00 per unit.

It is impossible to match the invoice with the contract. The invoice appears to be a bill for just one item for 12 months -  $12 \times \$102.00 = \$1,224.00$ . But the invoice states the service billed is for 4 and not 12 months. One unit for 4 months should cost \$408.00 not \$1,224.00.

#### Possible Overpayment

This is a potential overpayment.

DFAS paid the bill on August 15, 1997. The amount paid was \$1,224.00 - the amount billed. DFAS assumed that the bill covered all three units for 4 months. This may be an overpayment of \$816.00, since the invoice covered just one piece of equipment.

#### Circumvention of PPA

This payment may not comply with the PPA. While it took 163 days to pay this bill, the payment included no interest.

The dates used to compute interest due on this invoice appear to be false. In this case, the date stamp on the invoice was the determining factor used to cheat the vendor out of interest. The official DFAS invoice receipt date - recorded in IAPS - is July 23, 1997. That doesn't even square with the bogus date stamp on the invoice itself of July 31, 1997.

DFAS maintains that it first received the invoice on July 23, 1997. That is date the invoice was faxed to the center. But the invoice is dated March 4, 1997. What happened to it during the intervening 5 months - from early March until late July? Was the original thrashed and replaced with the special fax copy in late July?

#### Variance in Remit Addresses

The contract gives the company's official Chantilly, VA mailing address in Block 17a. The invoice, by comparison, provides three different remit addresses - 2 in Pittsburgh and 1 in Philadelphia. The check was sent to the Philadelphia address.

#### I-NET WANG

We examined 2 invoices from this company - No. 9747-014-003 and No. 9692-411-00048. In reviewing these transactions, we detected several problems as follows:

- No receiving reports
- "Lost" invoices
- Falsification of information in IAPS
- No time sheets or records to support services
- Unauthorized payment
- Variance in remit addresses

#### Invoice No. 9747-014-003

This invoice is dated June 27, 1997. It covers maintenance support by a field engineer and network administrator. The period of service covered by the invoice is April-May 1997. The total amount billed was \$24,514.00.

The invoice was date stamped July 14, 1997.

#### Receiving Report

The accounts payable file at Denver did not contain a receiving report for this invoice. The request for receiving report in the file was neither dated nor signed.

Following our visit, DFAS generated a document that may qualify as a receiving report. It is dated April 23, 1998. Although it is a request for receiving report, it contains all the information needed to certify receipt of goods and/or services. It is signed by an authorized government representative - Tara M. Curran - and certifies that the services billed were received and accepted on May 31, 1997.

#### Receiving Report - Discrepancies

The new receiving report contains several important discrepancies.

First, it reports that the field engineer, Mr. Ronnie W. Towne, worked 197 hours instead of the 198 hours billed. He took 1 hour of sick leave on April 25, 1997. As hard as it is to believe, we were told that this 1-hour discrepancy is the reason why this bill remained unpaid for an entire year.

Second, despite the year-long dispute over 1 hour of sick leave, Ms. Curran's certification recommended that the total amount billed - \$24,514.00 - be paid in full. She was unable to produce time sheets to prove that the services were, in fact, delivered, or to back up her claim about the 1 hour of sick leave - even though she was given weeks to locate them. It seems like this issue could have been resolved with one phone call. Were these services ever delivered?

Third, the invoice was "re-manufactured." It was given a new date of March 16, 1998 but still includes the disputed hour of sick leave. I believe the invoice was re-dated to circumvent the PPA. Even a new invoice receipt date of June 2, 1998 was entered in IAPS for this purpose. However, when the bill was finally paid in full on June 22, 1998, it included \$1,477.54 of interest. The PPA calculation dates appeared to be correct. The dates in IAPS may have been altered - again - because of all the scrutiny we directed at this transaction.

#### Invoice/Contract Mismatch

The contract is dated November 27, 1996 and had an effective date of October 1, 1996. It was signed by the contracting officer but not the vendor. It covered maintenance services by 1 field engineer and 1 network administrator for 6 months - from October 1, 1996 through March 31, 1997. The total award amount was \$93,372.06.

#### Unauthorized Payment

Since the contract expired on March 31, 1997 and the invoice covered services rendered in April and May 1997 - after contract expiration, this does not constitute a legal government obligation. The check issued by DFAS on June 22, 1998 is an unauthorized payment. The full amount - \$25,991.54 - should be returned to the Treasury and credited to the proper account.

#### Lack of Vendor Interest

Throughout the review of this invoice, we were told that the vendor never called to complain about non-payment of this very substantial bill. The company confirmed that fact. I-Net Wang said that it had no contact with DFAS about this invoice until May 1998 - after we started asking questions.

I-Net's apparent lack of interest in getting paid could have stemmed from the fact that the company knew full well that there was no valid contract to cover the invoice. For that reason, the company may have been reluctant to pursue payment.

Mr. Bill Ryan, the company's Comptroller and Vice President for Finance, offers a different explanation. He suggests that the bill "fell through the cracks" after I-Net was purchased by Wang and restructured internally. The new company was broken into two parts - one commercial and the other federal. He said this account receivable was misplaced in the commercial books. We asked him: How many other bills like this one also "fell through the cracks?" Mr. Ryan said our inquiry triggered a corporate review of the commercial books. As a result of this review, the company discovered \$1.3 million of "open" or unpaid bills, and the review is continuing.

#### Remit Address

The company's official mailing address in Bethesda, MD is identified in block 17a of the contract document. That is the address to which the check should be sent. This same address appears on the invoice. The check - EFT payment - was sent to an entirely different Virginia address.

#### Invoice No. 9692-411-00048

This invoice is dated October 18, 1996. It covered the delivery of 11 pieces of audio-visual equipment. This equipment was supposed to be delivered to SAM's warehouse in Arlington. The total amount billed was \$12,354.00.

The invoice itself was not an original. It was an "original duplicate invoice." DFAS said the original was "lost." The duplicate invoice was date stamped April 4, 1997. That means it took the invoice almost 6 months to reach the Denver center.

#### Receiving Report

The accounts payable file at Denver did not contain a receiving report. In fact, on August 18, 1997, SAM notified DFAS not to pay this bill because it could produce no proof of delivery. At that point in time, the bill had already been paid.

#### On-Site Inspection

On July 27, 1998, we located equipment in SAM that matched the description of the equipment billed on the invoice. However, without any serial numbers, it is impossible to know whether this was the same equipment ordered by the contract and billed on the invoice. There was one minor discrepancy, as well. The invoice charged \$1176.00 to install 3 "Livecam Plus Picture Tels" at \$392.00 each. Only one was actually installed.

#### Invoice/Contract Match

The items ordered in the contract appear to match up perfectly with the items billed in the invoice.

#### Payment

The bill was paid in full on August 6, 1997 - 291 days after it was submitted. The payment included an interest penalty of \$206.83. The PPA interest computation dates displayed on the voucher are suspect.

The invoice receipt date of April 4, 1997 makes no sense - given the invoice date of October 18, 1996. The invoice in the accounts payable file was a duplicate - not the original. The vendor confirmed that it sends DFAS multiple copies of the same invoice. This suggests that the K file to support the October 18th delivery date. That date was fabricated.

In all probability, these dates are phony and were used to circumvent the PPA.

#### Remit Address

The remit address specified in the contract is identical to the address used on the voucher and the check.

#### INVINCIBLE OFFICE FURNITURE

This purchase involves two invoices: one from Invincible Office Furniture - No. 74294 - and the other from Domore/DO3 Systems - No. 167807. These invoices covered the purchase of modular furniture for SAM's Strategic Transition Office.

In reviewing these two transaction, we detected several significant deficiencies as follows:

- No receiving reports
- "Back-dated" documents
- Unexplained delays in verifying receipt
- Furniture ordered and paid for but not delivered
- Falsification of dates in IAPS
- Variance in remit addresses

#### Invoices

There were two invoices totaling \$41,560.47 as follows:

- Invincible Office Furniture invoice No. 74294, dated June 9, 1997, for modular furniture totaled \$36,941.23
- Domore invoice No. 167807, dated May 28, 1997, for 18 chairs totaled \$4,619.24

The Invincible invoice was date stamped June 16, 1997, while the Domore invoice had two date stamps: June 10, 1997 and October 6, 1997.

#### Receiving Reports

The accounts payable files for these invoices did not contain a receiving report, However the file contained at least 4 different request for receiving reports for the Invincible invoice but none for the Domore invoice.

On the initial request for receiving reports of June 6, 1997 and August 4, 1997, SAM recommended that DFAS not pay the Invincible invoice because it had absolutely no proof of delivery. The August 4 report was subsequently back-dated on or about November 6, 1997, after we began asking questions. The back-dated reports were signed by an authorized government representatives - Robert L. Fisher (customer) and Mike Aquila - who certified that the goods were received and accepted on June 6, 1997. Several documents in the file, including a job work order covering the delivery and installation of the modular furniture, are consistent with the June 6th delivery date. Documents in the file also indicate that the 18 chairs from Domore were

delivered on the same day.

#### Unexplained Delay in Verifying Receipt

Why did it take SAM five months - from June 6, 1997 until November 6, 1997 - to verify delivery of this furniture?

This problem is particularly difficult to understand for several reasons.

First, documents in the file indicate that Mr. Mike Aquila - the person responsible for verifying receipt - contacted the customer who had the furniture, Mr. Bob Fisher, on several occasions. Mr. Fisher said if Mr. Aquila had called him, he would have told him he had the furniture and was satisfied with it. This apparent miscommunication is particularly difficult to understand because both Mr. Fisher and Aquila serve in the same organization, SAM, and their offices could not be more than 30 yards apart along the same Pentagon corridor.

Second, with not much more than a invoice and phone, an intern in Senator Grassley's office, Mr. Chad Barth, succeeded in pinpointing the location of the furniture in about five minutes.

This miscommunication is just another glaring example of Pentagon waste. SAM's failure to verify receipt in timely manner cost the taxpayers \$1,386.22 in interest penalties paid to Invincible plus the \$111.01 in interest still owed to Domore. A quick and easy phone call could have solved the problem and avoided such a senseless waste of money.

#### Invoice/Contract Mismatch

Both the Invincible and Domore contracts were signed on May 15, 1997 and called for delivery by June 2, 1997. Delivery was to be made to the SAM warehouse in Arlington, VA. The total award amount was \$41,778.93. The contract was modified on May 22, 1997. The modification shifted delivery to the customer's office and altered the list of modular furniture to be delivered by Invincible, reducing the cost of the contract by \$218.55 to a new total \$36,941.18. The Domore order remained unchanged.

A major problem arose when we attempted to reconcile the items delivered with the items ordered in the contract.

The equipment list attached to the May 22, 1997 contract modification signed by Mr. Bob Fisher tracks closely with the list attached to the original contract with several minor differences - differences noted by Mr. Fischer. However, it is impossible to match the "Job Work Order" of June 6, 1997, which lists the furniture actually delivered, with the "Revised Equipment List/Quotation" attached to the contract modification.

There appear to be a number of major discrepancies - missing pieces of furniture.

For example, the contract called for delivery of 2 Q-2443 acoustical raceway panels at \$472.00 each. None are listed on the Job Work Order. The contract called for the delivery of 18 Q-2468 acoustical raceway panels at \$570.00 each. The job work order indicates only 10 were delivered. The contract called for the delivery of 21 Q-SC68 square fabric posts for \$1,057.88. The Job Work Order, by comparison, indicates that only 8 Q-SC68 posts were delivered. Similarly, the contract called for the delivery of 15 Q-TC68 Fabric trim ends for \$279.00. However, only 8 were delivered. A line-by-line comparison clearly shows a large number of missing items.

In addition, the Job Work Order included at least one item not listed in the contract.

Since there are no dollar amounts shown for each individual item or grand total given on the Job Work Order, it's impossible to complete reconciliation and verify that Mr. Fischer got what he ordered.

We questioned Mr. Fisher about the missing items on March 19, 1997. He said the discrepancies were due to packaging multiple items in single cartons. But a check with Invincible laid that issue to rest, and, in fact, raised the possibility of more discrepancies. While Mr. Fisher says the furniture meets his needs, the evidence suggests that furniture was ordered and paid for that was never delivered and may have been unneeded for the layout.

#### Circumvention of PPA

The handling of the Invincible and Domore invoices help to highlight how DFAS manipulates information in IAPS to cheat vendors out of interest penalties that are, in fact, due.

Both the Invincible and Domore contracts were signed on the same day - May 15, 1997. The invoice dates are nearly identical - May 28th for Domore and June 9th for Invincible. Both delivered the goods to the same customer on the same day - June 6, but the dates for each transaction reflected in IAPS, which are used to calculate interest on the PPA, are totally different.

For invincible, the delivery date in IAPS is June 6, 1997 and the invoice receipt date is June 16, 1997. Those appear to be essentially correct. As a result, Invincible's check dated January 29, 1998, included substantial interest penalties.

For Domore, by comparison, the service delivery date in IAPS is October 16, 1997 and the invoice receipt date is October 6, 1997. Both dates appear to be fictitious. As a result, Domore's check dated November 10, 1997 included no interest penalty. The origin of the October 6th receipt date is unknown. There is nothing in the file to support it. The invoice has two date stamps: June 6 and October 6, 1997. The later one was probably placed on the invoice

at the last possible moment to preclude an interest payment. The multiple date stamps in this case are difficult to understand, since Domore submitted at least 4 different copies of this invoice to DFAS. An interest penalty of \$111.01 is due and should be paid immediately.

#### Remit Addresses

The Invincible contract provides a remit address in Manitowac, WI. The check, however, was sent to a different remit address in Manitowoc, WI that appears on the invoice. The Domore contract provides a remit address in Elkhart, IN. However, the Domore check - EFT Payment - was sent to a bank account in Illinois. The origin of that address is unknown, since the Domore invoice provides yet another different remit address in Chicago, IL.

#### LEIGHTRONIX, INC.

We reviewed one invoice from this company - invoice No. 970000207. In examining this invoice, we detected one major problem:

--Falsified information in IAPS

#### Invoice

This invoice is dated February 19, 1997. The invoice covers testing services performed in the Pentagon's National Military Command Center (NMCC). Mr. David Leighton traveled from Holt, Michigan to the NMCC "to check voltage and wave-form levels" in anticipation of a planned up grade of the "DISIDS control systems." The amount billed on the invoice is \$1,900.00

The invoice itself bears at least 3 dates stamps as follows:

--February 24, 1997.  
--March 5, 1997  
--March 17, 1997.

#### Receiving Report

The accounts payable file at the Denver center did not contain a receiving report. However, it did contain several conflicting documents that could qualify as receiving reports.

First, there is a signed copy of the 1449 contract document. While the signature is unreadable and appears in the wrong block, it references invoice No. 970000207 and is dated February 18, 1997. That date is fully consistent with all the documents in the file, including independent statements by the contractor, Mr. Leighton, and the customer in the NMCC, Mr. Alfredo S. Hernandez.

Second, there is a request for receiving report dated March 21, 1997. It is undated and unsigned with this notation: "Can not verify receipt of goods/services . . ."

Third, another SAM document in the file - a fax transmittal sheet, dated May 2, 1997, states: "the contractor provided the service on 18FEB97." This was sent to DFAS/Denver.

Fourth, there are two versions on the request for receiving reports dated August 4, 1997. Both are signed by an authorized government representative, Mike Aquila. Both indicate contact with the customer in the NMCC, Mr. Hernandez. One does not certify receipt and acceptance of services. The other does - effective April 15, 1997. The certification date appears to have been back-dated on to the document. This document was created after we started asking questions.



We examined the same document in August, and it included no such date.

#### Invoice/Contract

The contract was signed on January 31, 1997. It is signed by the government contracting officer but not the vendor. The total award amount is \$1,900.00.

The scheduled delivery date was March 7, 1997.

The amount and services billed on the invoice appear to match perfectly with the services and amount authorized in the contract.

#### Circumvention of PPA

This invoice was finally paid on December 3, 1997 - 286 days after the bill was first submitted for payment. The check included \$69.00 in interest penalties.

Unfortunately, the dates used to compute the interest penalties appear to be fabricated. The dates used to compute interest penalties - as displayed on the voucher - indicate that the invoice was received on March 17, 1997, and the service was delivered on April 15, 1997. Those dates appear to be fictitious. They are not supported by legitimate documentation in the accounts payable file. They were manufactured to cheat the vendor out of interest due.

The deception and falsification of dates is highlighted by a document provided by Mr. Leighton. This is a DFAS/Denver form letter addressed to Mr. Leighton. It is dated August 22, 1997. It states: "Our records indicate no invoice has been received . . . ." That appears to be a blatant lie. DFAS records clearly show otherwise. First, there is the DFAS/Denver date stamp of February 24, 1997 on the invoice. Second, there are the request for receiving reports of March 21, 1997 and August 4, 1997. These indicate the invoice was in IAPS prior to March 21st. Third, a voucher was prepared for payment in late August, including \$34.89 in interest penalties. The voucher was subsequently voided or cancelled. DFAS then waited another three months before paying the bill. Why?

Documents in the accounts payable file indicate the invoice was received on February 24, 1997, and the service was actually delivered on February 18, 1997. Using the correct dates, the interest penalty should have been \$86.44. An additional \$17.44 is due and should be paid to the company.

#### Remit Address

The contract provides a remit address in Holt, Michigan. The check was sent to that address.

### LIEBERT CORPORATION CUSTOMER SERVICE & SUPPORT (CS&S)

We reviewed several invoices from Liebert CS&S but focused on invoice No. MI1487690. In examining this invoice, we uncovered major discrepancies as follows:

- Invalid receiving report
- Services charged to wrong contract
- Duplicate payment

#### Invoice

The invoice is dated April 2, 1997. It covers monthly maintenance for March 1997 on contract No. F4964297M0199. The total amount billed is \$624.36.

The invoice is date stamped April 7, 1997.

#### Receiving Report

The accounts payable file at Denver contained a DD-250 receiving report, but it is not a valid report. It covers maintenance of "uninterruptible power" for March 1997 at \$5,578.00. It identifies Liebert CS&S as the vendor but references an incorrect contract No. - FA441697MF025. The space provided for the invoice number is blank. The invalid DD-250 is signed by SRA Nicole Brunage of "Contract Services" on March 31, 1997.

The request for receiving report, dated August 4, 1997, is marked with LTC Barner's rubber stamp. The line for the date the services were received and accepted is blank.

#### Invoice/Contract Match Up

The correct contract - No. F4964297M0199 - is dated October 9, 1996. Its effective date is October 1st. It is signed by the government contracting officer but not the vendor. The total award amount was \$7,492.32 or \$624.36 per month. It covered on-site maintenance on four power distribution units. The serial numbers of each unit is identified in the statement of work. The period of service is October 1, 1996 through September 30, 1997.

The services billed on the invoice, including serial numbers, appear to match up perfectly with the contract.

### Duplicate Payments

#### Payment No. 1

DFAS/Denver prepared this invoice for payment on at least 4 different occasions - in May, June and twice in August. We know it was paid at least twice, so this is a duplicate payment.

The duplicate payment occurred because the first payment was charged to the wrong contract - No. FA441697MF025. This was also a Liebert CS&S contract but applied to other maintenance work. If the pay technician had checked this contract, that person would have quickly realized that it was impossible to match the invoice with the contract.

The first payment was made on June 4, 1997 on voucher No. D700053134 by check. This payment was charged to contract No. FA441697MF025. The total paid was \$625.58, including \$1.22 of interest. The interest computations dates were partially incorrect. The invoice receipt date displayed on the voucher is April 24, 1997. This does not match with the date stamp of April 7, 1997. The service delivery date of March 31, 1997 seems correct, since this was a service bill for the month of March.

#### Payment No. 2

The invoice was prepared for payment again - on August 26, 1997 - on voucher No. D700085532 for \$636.73, but this voucher was voided or cancelled for unknown reasons and replaced by another one - No. D700087094 - issued on August 28th. This was the duplicate payment. The total amount paid - \$636.95, including \$12.59 of interest. The PPA interest computation dates displayed on the voucher appear to be correct - as compared to the dates on the first voucher. This is the payment that was cleared with LTC Barner's rubber stamp.

The first payment should be returned to the Treasury and credited to the correct account. No demand letter was issued, but the company has acknowledged receipt of the duplicate payment and returned the money. The refund check is dated July 30, 1998, and the money was credited to the correct accounts on August 5, 1998.

#### Variance in Remit Addresses

The remit address shown on the incorrect Liebert CS&S contract was in Hanover, MD. The first payment - a check - was sent to the Chicago, IL address given on the invoice. The remit addresses given on the correct Liebert CS&S contract and the invoice were the same Chicago, IL address. This is the address to which the first check was sent. However, the second payment - an EFT payment - was sent to a different address in IL.

### MICROAGE CORPORATE SYSTEMS CENTRE

We examined one invoice - No. 418437 - from this company. In reviewing this invoice, we detected several deficiencies as follows:

- Bill took 134 days to pay but earned no interest
- Incomplete and conflicting receiving reports
- Deliveries don't match contract order
- Cheaper units substituted for more costly units
- Received 4/9" Panasonic color monitors versus 2 ordered (\$680.00 each)
- Received 2/20" Sony color monitors versus 4 ordered (\$1,333.00 each)
- Panasonic color TV monitor missing for 3 weeks
- Purchase of excess spares to bypass arbitrary limits on "micropurchases"

#### Invoice

This invoice was dated July 23, 1997. It covered the delivery of 4 BTS-901Y 9" Panasonic Color TV Monitors at 680.00 each or \$2,720.00 and 2 PVM-2030/BS 20" Sony Color TV Monitors at \$1,333.00 each or \$2,666.00. These were purchased for use in the National Military Command Center (NMCC). The bill totaled \$5,386.00.

The invoice was date stamped September 18, 1997. That means it took 55 days to reach the Denver center. Information provided by the vendor indicates that duplicate invoices were submitted to DFAS on several occasions.

#### Receiving Report

The accounts payable file at Denver contained one document that could qualify as a receiving report. Unfortunately, this document presents a very confusing picture.

The document in question is a form 1449 signed by the customer in the NMCC, Mr. Alfredo S. Hernandez. He indicated that the goods were received and accepted on November 7, 1997, but the receipt covered a "partial payment only." It referenced invoice No. 419444 that was a duplicate of the original invoice - No. 418437. Invoice No. 419444 covered just 2 Sony color monitors. The invoice number - 419444 - is crossed out and replaced with the original invoice number - 418437 - that covered all 6 items. Another handwritten note on the same document

indicates that 2 of the 4 Panasonic color monitors ordered were received on September 28, 1997. These cryptic notes may indicate that all 6 units were received and accepted. We don't know.

The file also contained a request for receiving report dated October 10, 1997. This document is undated, unsigned, and uncertified.

#### Invoice/Contract Mismatch

The contract is dated May 19, 1997. It is signed by the contracting officer but not the vendor. It authorizes the purchase of 2 BTS-901Y 9" Panasonic Color Monitors at \$1,333.00 or \$2,666.00 and 4 PVM-2030 20" Sony Color Monitors \$680.00 or \$2,720 for a total contract award of \$5,386.00. These items were to be delivered directly to the customer by June 10, 1997.

A problem arises when the invoice is compared with the contract. There is a mismatch between the order and the delivery.

The invoice covered the delivery of 4/9" Panasonic color monitors at \$680.00 or \$2,720.00 and 2/20" Sony color monitors at \$1,333.00 or \$2,666.00 for a grand total of \$5,386.00. The total amount billed matched the total contract award amount - exactly, but the mix of monitors delivered was very different. The NMCC apparently received 4 9" Panasonic color monitors versus the 2 ordered; and 2/20" Sony color monitor versus the 4 ordered. The NMCC did not receive what it ordered.

Assuming the unit prices charged on the invoice - and paid by the government - are accurate and correct, the order authorized by the contract would have actually cost \$6,692.00. It appears that the quantities were shaved to meet the contract ceiling amount. The NMCC got more of the cheaper Panasonic units and fewer of the more costly Sony monitors.

The bill was paid in full - \$5,386.00 - on December 4, 1997 - with no interest.

#### On-Site Verification - Missing TV Monitor

Since a color TV monitor is a pilferable item and deliveries may have been altered to cut costs, we attempted to actually locate these items during a visit to the NMCC on June 1, 1997.

We began the meeting by asking the customer, Mr. Hernandez, to call up his property management system - known as APMS - on the computer. Mr. Hernandez identified the items listed in the APMS that were covered by Microage invoice No.418437. He provided individual serial numbers for each of the items covered by the invoice. Since serial numbers were not given

on the invoice, we had to rely on the information provided by Mr. Hernandez. The APMS indicated that all 6 units were located in the NMCC storeroom - RM 5E972 - as operational spares.

On visiting the storeroom, we were able to match the Sony serial numbers provided by APMS with the units in storage. However, instead of 2 Sony monitors, there were actually 4 on the shelf. We also located 3 of the 4 Panasonic monitors and matched up the serial numbers. However, one Panasonic monitor was missing and remained unaccounted for until June 26th or more than 3 weeks. A complete search was conducted during our visit. The missing unit was finally located on a camera stand in the Crisis Action Center. Mr. Hernandez was unable to provide a satisfactory explanation as to why it took 3 weeks to find it.

Was the missing Panasonic color monitor in the NMCC during our June 1st visit? Was it simply misplaced? Or did someone have it at home and return it after questions were asked? The NMCC's inaccurate and incomplete property management records means highly pilferable items like a Panasonic color TV monitor are vulnerable to theft. "If you don't know what you have, you don't know what's missing."

#### Excess Spares

We also asked Mr. Hernandez about all the excess spare monitors in the store room. He said they are needed because these units run 24-hours a day. He also told us that the excess spares were bought to push the total buy over the \$2,500.00 ceiling on "micropurchases." He said the company would not accept a credit card purchase, and the dollar-limit on contract purchases with the Form 9 purchase order had to exceed \$2,500.00. So he bought extra spares to push the cost of the order over the top and get around the rule.

#### Remit Address

The check was sent to the remit address specified in the contract.

### MONROE SYSTEMS FOR BUSINESS, INC.

We reviewed at least 5 invoices from this company. Each was handled in roughly the same manner, so we selected one to highlight DFAS' late payment practices - No.951207. In examining this invoice, we detected several problems as follows:

- No receiving report
- Invoice/Contract Mismatch
- Contract authorized 45,000 copies/year
- Invoice includes rates not authorized in contract
- "Loss" of original invoice
- Falsified data in IAPS
- Variance in remit addresses

#### Invoice

The invoice is dated February 28, 1997. It covers monthly maintenance on one copy machine - model RL932DX with serial number E260907 - for the period February 1, 1997 through February 28, 1997. The total amount billed is \$53.92. The copy allowance of 45,000/year and the overage rate of \$.0144/copy are noted. Since there were no copies in excess of the allowance, there were no charge for overage.

The invoice is date stamped August 11, 1997. It took 6 months to reach the center.

#### Receiving Report

The accounts payable file at the Denver center contains no receiving report.

The file did contain a request for receiving report. It was signed by an authorized government representative, Mr. Mike Aquila, but it is undated and fails to certify that the services were received and accepted on a specific date.

#### Invoice/Contract Mismatch

The contract was signed on October 4, 1996. Its effective date was October 1, 1996. It is signed by the contracting officer but not the vendor. The total award amount is \$647.04 or

\$53.92 per month for maintenance on the copier identified in the invoice - serial number E260907; Model number RL-932DX. The cost covers up to 45,000 copies per year.

The contract performance period is October 1, 1996 through September 30, 1997.

The contract authorized the expenditure of \$647.02 per year on this particular copier for up to 45,000 copies per year - but no more. What would have happened if the copy allowance had been exceeded? The invoice indicates that the overage rate was \$.0144/copy. Unfortunately, overage charges were not authorized in the contract. If the allowance had been exceeded, there would have been an over-obligation. None of the Monroe invoices we examined billed for overage but the potential for a significant problem exists. And it seems to typify all DOD copier contracts.

#### Circumvention of PPA

This bill was paid in full on September 4, 1997 - with no interest - even though it took a total of 190 days to pay. A total of 190 days from invoice to payment clearly qualifies as a late payment.

DFAS circumvented the PPA and cheated the vendor out of interest by allegedly "losing" the original invoice and using a phony invoice receipt date on a subsequent or "reprint" copy. The date stamp on the invoice "reprint" is August 11, 1997. That is the official invoice receipt date displayed on the payment voucher and recorded in IAPS. This the PPA driver in this case. Other information in the file proves that this is a totally fictitious date.

We know the date stamp is false for several reasons. First, this invoice was listed in the request for receiving reports of August 4, 1997. That means it was received in the Denver center well in advance of official August 8th receipt date. Second, how could it possibly take 6 months to reach the Denver center? Third, the invoice itself is a "invoice reprint." It is not the original copy. It is a copy of the original - probably one of many sent to Denver after the bill became delinquent. What happened to the original invoice? Was it trashed?

The service delivery date of February 28, 1997 displayed on the voucher, by comparison, appears to be correct, since this was a service charge for the month February.

We attempted unsuccessfully to contact the vendor to verify this information. A letter and possibly 20 follow up calls went unanswered

#### Variance in Remit Addresses

The remit address given on the contract is in Arlington, VA. The check, however, was sent to an entirely different remit address in Philadelphia, PA given on the invoice.

## MOTOROLA SPACE AND SYSTEMS TECHNOLOGY GROUP

We reviewed at least 5 invoices from Motorola but chose to focus on just 3 that seemed to need special attention - No. 7016034, 7016190, and 7016281. In examining these invoices, we detected several major deficiencies as follows:

- Bills paid without invoices
- Bills paid without valid receiving reports
- Receiving report provided by contractor
- Deliveries never verified

### Invoices

The accounts payable files at the Denver center did not contain the three Motorola invoices, but all three bills were paid in November 1997 - nonetheless.

When we asked for copies of the invoices, we were told that they did not exist. Motorola was authorized to substitute DD-250 receiving reports for invoices - provided they included all pertinent information. A review of the 3 surrogate bills suggests the possible existence of 3 Motorola "invoices" for \$33,000.00 as follows:

- No. 7016034, dated July 18, 1997, for \$3,000.00
- No. 7016190, dated August 1, 1997, for \$15,000.00
- No. 7016281, dated August 15, 1997, for \$15,000.00

Two of the surrogate invoices are labeled "original invoice." One is labeled "file copy."

The 3 "invoices" covered the delivery of 11 "improved performance upgrade kits," Model No. 78-P35560N, at \$3,000.00 each for a grand total of \$33,000.00.

### Receiving Reports

The accounts payable files contained documents that might have qualified as receiving reports - had they not been provided by Motorola.

The reports in question are the DD-250 forms that also served as surrogate "invoices." Even though the DD-250's were supplied by Motorola, two of the three reports (No. 7016034 and No. 7016190) may bear the signature of an authorized government representative. While the names are unreadable, both signatures are dated October 16, 1997 and certify "acceptance" of the items listed on each "invoice." There is no signature and no certification on the third "invoice" - No. 7016281. The fax marks on these documents indicates they originated with the vendor.

A receiving report provided by the vendor does not constitute a very independent check on deliveries. It cannot qualify as a receiving report. Proof of delivery must come from an independent government official.

The accounts payable files also contained copies of the request for receiving reports dated October 10, 1997. The ones for "invoice" No. 7016034 and No. 7016190 are totally blank - unsigned, undated, and uncertified. However, there are three different versions for "invoice" No. 7016281. One certifies that the goods were received and accepted on October 16, 1997 and is signed by an authorized government representative, Ms. Nicole M. Dye. Another is uncertified and states that the goods were "not received as of 10/31/97" and is signed by a different government representative, Mr. Mike Aquila. The third one is totally blank.

### Invoice/Contract Match

The contract is dated July 3, 1997. It is signed by the contracting officer but not the vendor. It authorizes the purchase of 21 "Improved Performance 802.3 Upgrade Kits," Model No. 78-P35560N, at \$3,000.00 each or a grand total of \$63,000.00. These kits were to be delivered to the SAM warehouse in Arlington by August 8, 1997.

The "invoices" cover the delivery of 11 of the 21 kits and appear to match up with the contract.

### Compliance with PPA

Since there are no valid receiving reports and no valid invoices in the files, it is impossible to determine if these transactions comply with the PPA. However, the PPA computation dates displayed on the payment vouchers appear to be reasonably correct with one exception. The invoice receipt date for No. 7016190 is September 17, 1997. That doesn't quite fit. It suggests the "invoice" took 48 days to reach the center. Since the word "file copy" appears on the "invoice," we think it is reasonable to assume that the original and other copies were "lost" before DFAS decided to retain one with a fax date.

### Remit Address

The contract provides a remit address in Dallas, TX. All 3 checks were sent to that address.

### On-Site Inspection

We have been told that the kits are embedded in computers operated by the National Security Agency, but we have been unable to locate either the equipment or customer to verify receipt of the goods.

## OPENWARE TECHNOLOGIES, INC.

We reviewed one invoice from this company - invoice No. 97022829. In examining this transaction, we detected several significant problems as follows:

- Invoice/Contract mismatch
- Billed services lie outside contract period
- Unauthorized payment
- Falsification of information in IAPS
- Invoice tampering
- Voucher destroyed to hide paper trail

### Invoice

The invoice is dated February 28, 1997. It covers the delivery 4 Solaris software packages with license fee for \$8,500.00; software support for September 15, 1996 through September 14, 1997 for \$3,750.00; and shipping and handling charges of \$50.00. The total amount billed is \$12,300.00.

The invoice itself bears at least two date stamps - March 31, 1997 and May 1, 1997.

### Receiving Report

The accounts payable file at the Denver center did not contain a receiving report.

The file does contain two versions of a request for receiving report dated August 4, 1997. Both are signed by an authorized government representative, Ms. Nicole M. Dye. But only one certifies that the goods and services were received on a specific date - February 28, 1997. There is a large question mark next to the certification date. The one without the certification had this handwritten note at the bottom of the page: "This information was faxed to DFAS on 10July97 at 0843."

### Invoice/Contract Mismatch

The contract is dated April 1, 1997 and took effect on that date. It is signed by the contracting officer but not the vendor. It authorizes the purchase of 4 Solaris software packages with license fee for \$8,500.00 - to be delivered by April 30, 1997; software support from April 1, 1997 through September 30, 1997 for \$3,750.00; and shipping and handling charges of \$50.00. The total award amount was \$12,300.00

The dollar amounts billed match up well with the amounts authorized in the contract, but the dates on the invoice and contract are totally out of sync. First, the invoice is dated February 28, 1997 - one month before the contract was signed on April 1st. Second, the software support billed on the invoice extends from September 15, 1996 through September 14, 1997 - 5.5 months of the service lie outside of the contract. Under the law, this entire bill may not constitute a legal government obligation. At a minimum, payments for services performed prior to the effective date of the contract would be unauthorized payments. Third, the contract authorized software support for a six-month period - April 1 through September 30th - but authorized only enough money to cover 5 months -  $5 \times 750.00 = \$3,750.00$ . It's one month short.

### Circumvention of PPA

The handling of this invoice appears to show how DFAS is manipulating - and even falsifying information in IAPS - to avoid and/or reduce interest penalties under the PPA.

### First Voucher

Initially, this bill was prepared for payment on voucher no. D700094145 dated September 10, 1997. This payment included an interest payment of \$361.51 - presumably using the correct PPA computation dates in the file. Did someone intervene to block this interest payment? This voucher was voided or cancelled because of an "invalid invoice receipt date." A handwritten note on the void voucher states: "should be September 3, 97 (fax date)." The origin of this date is unknown and is unsupported by any documentation in the file.

### Second Voucher

Then about a week later - on September 16th, the bill was prepared for payment a second time on voucher No. D700097898. This payment included no interest penalty - presumably using the bogus September 3rd invoice receipt date. This voucher was also voided because of an "invalid invoice receipt date."

### Third Voucher

The bill was apparently prepared for payment a third time on voucher No. 700099100 dated September 18, 1997 - with no interest penalty. This voucher did in fact generate a U.S. Treasury check dated September 18th in the amount of \$12,300.00. When we requested a copy, we were told the voucher had been "destroyed."

DFAS appears to use the void procedure to hide the paper trail on the falsification of information in IAPS. Since all the vouchers underlying this particular payment were either



destroyed and/or voided, we have no way of knowing which dates were used to calculate interest under the PPA.

#### Senator Grassley's Inquiry

On December 3, 1997, Senator Grassley asked this question: "The Openware Technologies invoice was not scheduled to be paid until 10/3/97 - more than seven months late. Yet the government paid no interest. Why?"

#### Original Voucher Destroyed

Internal DFAS documents indicate that Senator Grassley's inquiry triggered an internal review at the Denver center. As a result, the original voucher - No. D700099100 - "was pulled from the file room" for review. At this point, DFAS documents indicate that the original voucher was "inadvertently destroyed." It may have been destroyed because it showed that the PPA computation dates were blatantly false, and the certifying official, who signed it, did not want to be held accountable.

Under existing regulations, DFAS is required to retain payment vouchers for at least 6 years. Why was this document destroyed?

#### Dummy Voucher Created

At Senator Grassley's request, the original voucher was "reconstructed," using electronic files buried in IAPS. DFAS created a "dummy" voucher. This document reveals several important facts - if true and accurate.

First, it shows that the invoice was charged to the wrong contract. It was charged to contract No. F4964297PO256 - A National Computer Warehouse contract - instead of contract No. F4964297PO265. Second, the PPA computation dates displayed on the voucher are: Invoice receipt date - May 1, 1997; And service delivery date of August 18, 1997. Since the bill was paid on September 18th and the service delivery date was August 18th, DFAS figured no interest was due. DFAS fabricated bogus dates to circumvent the PPA. Those dates are not supported by any documentation in the accounts payable file. They were manufactured to circumvent the PPA. An internal DFAS document admits: "The original payment was made using the wrong dates according to the PPA." If Senator Grassley had not raised questions, the false dates would have remained in effect and no interest would have been paid.

#### Special Interest Payment

Due to the "high level of visibility," an order was given to correct the problem. Pay technicians at the Denver center were told to "ensure that the interest owed was paid as soon as possible." A special interest payment voucher was approved on February 19, 1998. The vendor was paid the interest due - \$749.27 - using the correct dates according the PPA. The dates displayed on the voucher were: Service delivery date - February 28, 1997; and invoice receipt date - March 31, 1997. These dates accurately reflect information contained in the accounts payable file.

Since the accounts payable file contained the correct dates from the very beginning, why weren't these dates used in preparing the original voucher?

#### Remit Address

The checks were sent to the remit address specified in the contract.

## PROFESSIONAL PRODUCTS, INC.

We reviewed a number of invoices from this company but focused on one - No. 115292. In examining this transaction, we uncovered several problems as follows:

- Invoice/contract mismatch
- Items delivered were not ordered
- Goods delivered to SAM warehouse on May 23, 1997
- Goods not delivered to customer in Pentagon until August 1, 1997
- Erroneous information in IAPS

### Invoice

The invoice is dated May 23, 1997. It covers the delivery of 9 Barco projector CRT's at \$1,195.00 each. The total amount billed was \$10,755.00.

The invoice is date stamped May 30, 1997.

### Receiving Report

The accounts payable file at the Denver center contained a document that could qualify as a receiving report. It is a form 1449. It is signed by the customer, Mr. Alfredo Hernandez, and gives a receipt date of August 1, 1997. Mr. Hernandez also signed a copy of the invoice. It states: "Received 8/4/97" followed by his signature and another date - 8/1/97.

The file also contains a copy of the request for receiving report dated August 4, 1997. This document is signed by an authorized government representative, Mr. Mike Aquila, but it is undated and uncertified. A handwritten note states: "Items received in office 8/7/97; originally delivered to warehouse on ---- ? Faxed 1449 to DFAS 8/1/97."

### Invoice/Contract Mismatch

The contract is dated May 5, 1997. It is signed by the contracting officer but not the vendor. It authorizes the purchase of 9 Barco projector CRT's at a cost of \$1,195.00 each. The total award amount was \$10,755.00. These items were to be delivered to the SAM warehouse in Arlington, VA by June 2, 1997.

The prices and equipment billed on the invoice appear to match with the prices and equipment authorized in the contract - with one minor exception. The contract called for the purchase of 3 Barco projector CRT model numbers 7625562K, 3 model numbers 7625525K, and 3 model numbers 7625566K. The invoice, by comparison, indicates that 3 Barco project CRT model numbers 7625425K were delivered. There was no order for this particular model. The model numbers for the other six units listed on the invoice match with those in the contract.

### Circumvention of PPA

Despite the fact that it took DFAS 96 days to pay this bill, the check, issued on August 27, 1997, included no interest. Interest was withheld because the delivery date in IAPS - August 1, 1997 - was within 30 days of the check date. We believe that the August 1st delivery date is incorrect.

The delivery date of August 1st was probably the date the goods actually reached the customer, Mr. Hernandez. However, this is probably not the date on which the vendor actually delivered the goods to the designated delivery point - the SAM warehouse in Arlington, VA.

### On-Site Inspection

We met with Mr. Hernandez on September 8, 1997 in an attempt to verify delivery for the 9 Barco projector CRT's.

During this meeting, we were provided with a key document - a packing slip - which clearly indicates that the 9 CRT's were delivered to the warehouse on May 23, 1997. The packing slip was signed "Rec'd by R. Johns, 5/23/97, 10:30." R. Johns is presumably a SAM employee assigned to the warehouse. We were also told that the warehouse faxed this document to DFAS.

Somehow, the 9 12" X 24" cartons containing the CRT's got "lost" or misplaced in the warehouse for over two months. Mr. Hernandez had to track them down himself. Mr. Hernandez tried to suggest that they were delivered to the warehouse "by mistake." In point of fact, the warehouse was the delivery point specified in the contract. So the vendor fulfilled all delivery obligations.

A failure to properly manage and control inventory within the warehouse is not the vendor's responsibility, and the vendor should not be penalized for such mismanagement.

Assuming the goods were, in fact, delivered on May 23rd and the invoice receipt date was May 30th, an interest penalty of \$112.61 is still due and should be paid to the vendor.

### Vendor Complaints

On May 14, 1998, Senator Grassley addressed a letter to the company to raise questions about the way this invoice was handled by DFAS. Mr. Jerry Weinberg, a company representative, called on May 26th in response to the letter.

Mr. Weinberg complained loudly about DFAS' late payment practices. He explained his company's follow up procedures on unpaid invoices. Copies of unpaid invoices are faxed to DFAS - not mailed. He said "numerous" copies of unpaid invoices are sent to DFAS. He figured that 30% of all invoices he sends to DFAS/Denver are "lost." Lost invoices are a big and continuing problem, he said. He is well aware of the PPA but doesn't worry about it.

The company's main concern is just getting bills paid. He said "he knows exactly what DFAS is doing to avoid interest payments. They repeatedly ask for copies of invoices then lose them to avoid paying interest. Then, when DFAS reaches a point where it thinks the bill must be paid, an invoice is date stamped - just prior to payment."

### Remit Address

The check was sent to the remit address specified in the contract.

### RGB TECHNOLOGY, INC.

We reviewed a number of invoices from this firm but chose to focus on just two - No. 4363 and No. 4434. In reviewing these transactions, we detected several problems as follows:

- Two different invoices for same order
- Altered prices
- No receiving reports
- Invoice/Contract mismatch
- Unauthorized purchase
- Mahogany desk purchased with emergency maintenance contract
- No management controls over furniture
- Variance in remit addresses

### Invoices

The original version of the invoice - No. 4363 - was dated May 27, 1997. It covered the delivery of two items: 1) A mahogany desk for \$595.00; and 2) 10 fast blow mini fuses at \$.80 each. There was no charge indicated for the fuses. The total amount billed was \$595.00. The original invoice was date stamped June 2, 1997.

Invoice No. 4363 was resubmitted for payment with a new number - No. 4434 - and a new date - June 27, 1997. In this instance, there is no charge for the mahogany desk - even though it was not paid until August 7, 1997. However, there is a charge for the 10 fast blow mini fuses - \$2.00 each or \$20.00 total. The second invoice is date stamped June 30, 1997.

### Receiving Reports

The accounts payable file at the Denver center did not contain a receiving report.

The files did contain three different request for receiving reports for June 6th, August 4th, and August 13, 1997. These documents provide conflicting information. One is rubber stamped and provides no certification date. The second one seems to indicate that the mahogany desk was received on May 27th. The third one indicates the fuses were delivered on June 27th. The customer, Mr. Alfredo Hernandez, signed copies of the invoices, indicating that the desk was received on May 10th and the fuses on May 25th.

### Invoice/Contract Mismatch

The contract is dated November 22, 1996. It is signed by the contracting officer but not the vendor. It authorized payments up to \$24,000.00 for on-site emergency maintenance on a long list of specific audio-visual equipment installed in the Pentagon's National Military Command Center (NMCC) and Video Recording Facility.

The contract states that repair parts may be purchased under this contract. The contract period is October 1, 1996 through September 30, 1997.

#### On-Site Inspection

We met with the customer in the NMCC, Mr. Alfredo S. Hernandez, on June 1, 1997, to verify delivery.

The contract provides no authority for Mr. Hernandez or anyone else to purchase a Mahogany desk from RGB Technology. The desk is clearly far beyond the scope of the contract.

Mr. Hernandez provided a copy of the "service contract purchase" order for the desk and fuses. It is dated April 11, 1997 and is signed by him. It was addressed to the company. It orders the mahogany desk, Model 10078, for \$495.00 and 10 fuses at no cost. The desk was ordered from a National Business Furniture catalogue where Model 10078 is listed for \$479.00. This desk was not purchased for use in the NMCC. In fact, this purchase was totally unrelated to the equipment listed in the contract. The mahogany desk was purchased for SAM's "OP" conference room renovation project. Colonel Edwin S. Goodale, Director of Operations, decided he wanted a new desk for his conference room and latched on to the nearest available contract. We were told that there was plenty of money left on the contract. He needed the desk. And Mr. Hernandez knew how to circumvent the process to get the desk for Colonel Goodale.

#### Lack of Management Controls

We verified the existence of the mahogany desk. It is actually a small computer stand with one center drawer. It had no bar coded serial number plate like all the furniture in the Senate. It was not listed in any property management system. We were only able to locate it since Mr. Hernandez had personal knowledge of its purchase and supervised its placement. Without Mr. Hernandez, we would never have found it.

#### Compliance with PPA

Although there appears to be some minor discrepancies in the dates used to compute interest under the PPA on both invoices, the amounts actually paid appear to be correct. The check issued for the desk on June 2, 1997 included \$4.02 of interest. It took DFAS 72 days to pay this bill. The \$20.00 check for the fuses, issued on September 8, 1997, earned \$.15 of interest. However, since it was under a \$1.00, none was paid.

#### Variance in Remit Addresses

The contract provides a remit address in Reston, VA. Both checks were sent to a different remit address in Reston, VA - the company address given on the invoice. The company address appearing on the checks was not identified as the remit address on the invoice.

### SUN MICROSYSTEMS, INC.

We reviewed a number of invoices from this company. Since they were handled in roughly the same manner, we chose to focus on two - No. DO993603 and No. DO93160 - Nexaming this invoice, we uncovered several significant problems as follows:

- Homemade invoice with no company logo or date stamp
- Ineffective service verification
- Illegal contract and unauthorized payments
- Impossible to match amounts billed with contract amounts
- Falsification of information in IAPS
- Invoice tampering
- Bill took 315 days to pay - Zero interest
- Interest penalty of \$440.18 is still due

#### Invoice

The invoice is dated May 26, 1997. It covers "system level support" and "SW obligation support" for May 1997. The total amount billed was \$9,235.90

The invoice itself has a very unusual appearance. It is not an original. It has no date stamp and no company logo. It is very different in appearance from other company invoices in files at the Denver center, which have official logos. Invoice No. DO993603 looks like a homemade invoice manufactured at the Denver center. It bears a "SUNSERVICE-FINANCE" fax date of March 6, 1998. Contact with the vendor indicates that at least three copies of this invoice were sent to DFAS/Denver. A company employee, Ms. Teresa Montalvo, reported that the company's invoices "constantly disappear at DFAS."

#### Receiving Report

The accounts payable file at the Denver center contains a document that could qualify as a receiving report. This is a form 1449. It is signed by an authorized government representative, Ms. Earlene Capers. Her signature is dated May 2, 1997. Unfortunately, it references an entirely different invoice "No. 35163150 for Oct-Jan97. It does not indicate that the services were received and accepted. Another form 1449 in the file, also signed by Ms. Capers, is dated May 31, 1997 and merely makes a vague reference to "monthly payment." The latter date may be correct, since this was a monthly service bill. The effective delivery date for the service should be May 31st.

The file also contains a request for receiving report for August 4, 1997. It is signed by an authorized government representative, Mr. Mike Aquila, but provides no certification and no specific date on which the service was delivered. When we questioned Mr. Aquila on June 26, 1998 about the basis for his signature on this document, he admitted that he had no first-hand knowledge about the service delivered. He had no documents or notes to back up his signature and had no idea where the equipment was located or who was directly responsible for it. He could not identify the customer. Despite his total lack of knowledge regarding the service delivered, Mr. Aquila's signature on this document gave DFAS the green light to pay the bill.

#### On-Site Inspection

It literally took several months, many phone calls, and several aborted meetings to locate the person responsible for the equipment being maintained under this contract. However, on July 14, 1998, we finally met with the customer, Sgt. Gilmore, who could verify actual delivery of the service.

Sgt. Gilmore is assigned to the Air Force Studies and Analysis Agency and identified the room numbers where the Sun Microsystems equipment is located. The equipment is being maintained under a new contract, but most of the equipment maintained under the old contract is still in place. He said 30 to 40 machines were involved, but he kept no records of the hours or actual work performed by the vendor. He had no time sheets. He said service is sometimes provided several times a week and sometimes several weeks will pass between visits.

#### Invoice/Contract Mismatch

The contract is dated December 23, 1996. It is signed by the contracting officer but not the vendor. Its effective date is October 1, 1996. It authorizes hardware and software maintenance support during the period October 1, 1996 through September 30, 1997. The total award amount was \$106,208.10 or \$8,850.68 per month. The monthly maintenance rate for May 1997 shown on the contract is \$8,867.30.

A contract modification was signed on April 16, 1997. It pushed the total award to \$108,496.10 - an increase of \$2,288.00. Four new machines were added to the list of equipment to be maintained from April through September. The new workload caused the monthly rate to increase - effective April 16th, but the new monthly rate is not specified. And it's very difficult to determine.

First, the contract authorized the performance of services beginning on October 1st -- three months before the contract was signed -- December 23rd. The effective date of the contract was back-dated to October 1st. Sun submitted a bill - invoice No. DO931650 - including \$26,322.60 for services performed in October through December 1996 and was paid for those

services on May 14, 1997. The entire amount may not constitute a legal government obligation, and the payment may not be authorized.

Second, it is very difficult - if not impossible - to match the invoice with the contract due to conflicting information. The amount billed for May 1997 is \$9,235.90. However, several different "adjusted maintenance fee" schedules provided by the vendor on June 17, 1998 indicate that the charge for May 1997 could have been as low as \$7,135.45 or as high as \$8,840.70 but well below the amount billed. Sun billed at the rate of \$8,840.70 a month in February, March, and April and was paid at that rate. The contract modification in April could account for some of the difference, but it is very difficult to construct the new monthly rate based on the information provided. We don't think that an enlisted pay technician at Denver could ever determine the correct amount.

#### Violation of PPA

The process used to pay this bill exposes the DFAS scheme for cheating vendors on interest penalties due. This is the smoking gun. It clearly and conclusively shows how DFAS deliberately and systematically falsifies information in IAPS to circumvent the PPA.

As of this very moment - today, DFAS maintains that this invoice was not received at the Denver center until March 6, 1998. This is the fax date on the re-manufactured or surrogate invoice. This is the date recorded on voucher No. D800076674. This is the date DFAS used to deny interest penalties on this bill. The bill was finally paid on April 6, 1998. Sun Microsystems was paid the amount billed on its invoice of May 26, 1997 - \$9,235.90. But not one penny of interest was included - even though it took DFAS 315 days to pay the bill.

The IAPS payment history - buried in electronic files - tells the true story on this invoice. We asked DFAS to recover these files and make them available to us for inspection. That document is attached to this report. A careful review of the document proves that DFAS knows that the invoice was not received in the center on March 6, 1998. DFAS knows that date is totally fictitious and fraudulent. That date was deliberately used to deny and withhold interest due. Official DFAS records show that this invoice was first received in the center on June 2, 1997 - not March 6, 1998.

And Sun's invoice No. D0993603 was no isolated case. At least 3 other invoices on the same contract were handled in roughly the same way: voucher - void - revoucher until the desired dates were created. Deliberate date tampering and falsification of data occurred on invoice numbers D0931653, D0993603, D0993608, and D0993606.

#### First Voucher

The first time DFAS prepaid this invoice for payment was on voucher No. D700068566 dated July 17, 1997. This voucher was voided - cancelled - and destroyed. So there is no printed voucher to examine. However, it is possible to reconstruct the record from electronic files.

The electronic files indicate that the PPA computation dates displayed on that voucher were: 1) invoice receipt date - June 2, 1997; and 2) service delivery date - June 24, 1997.

The invoice receipt date seems reasonable. Given the invoice date of May 26th, that suggests it took about a week to reach the center. That is excellent by DFAS standards. The service delivery date, by comparison, is a mystery. Documents in the file suggest that the service might have been delivered on May 2nd or May 31st. Since this was a bill for monthly services, the effective date should have been May 31st.

Now, why was this voucher voided and destroyed? It was allegedly voided because of an "invalid BNR" - for bill not received. There was a discrepancy of \$197.60 between the amount billed and the amount authorized for payment. This amount was deducted from the payment that was never made. But there is absolutely nothing in the file to support the non-existent discrepancy. The "BNR" discrepancy was pure fiction. The disputed amount is identical to the total amount "back billed" on another Sun invoice - No. DO993608, dated May 9, 1997.

We believe that the discrepancy was fabricated so that the invoice and voucher could be destroyed. The DFAS voiding process is like a laundry operation. It destroys the paper trail. It provides cover for the destruction of invoices with original date stamps and the creation of new invoices with new date stamps.

#### Second Voucher

The first voucher was destroyed in late July 1997.

DFAS then waited about 8 months to begin processing this invoice for payment a second time. When it was re-entered in IAPS on March 10, 1998, it was given a whole new set of PPA computation dates as follows: 1) invoice receipt date - March 6, 1998; and 2) service delivery date - May 30, 1997. These dates allowed DFAS to withhold the payment of interest penalties. They are also totally false.

The invoice receipt date of March 6, 1998 is the fax date on the re-manufactured invoice. This invoice was probably created at Denver - but possibly by the vendor - then faxed back and forth until a new receipt date was established. The service delivery date appears to be almost correct.

The second payment was to be made on voucher No. D800073712 dated March 30, 1998. Had the payment been made, the bill would have been paid in full - \$9,235.90. However, the invoice was voided on or about March 30th because: "receiving report invalid."

This void was just a minor hiccup. The "invalid" receiving report did not stand in the way of payment - at least not for very long. A week later the third and final voucher on this invoice was prepared.

#### Third Voucher

The third and final voucher - No. D800076674 - is dated April 6, 1998. It paid Sun Microsystems \$9,235.90 - the exact amount originally billed on May 26, 1997. The payment included zero interest.

No interest was paid because DFAS says this invoice was not received at the Denver center until March 6, 1998. The service delivery date reported on this voucher, by comparison, is probably correct - May 31, 1997.

Assuming the invoice receipt date of June 2, 1997 and the service delivery date of May 31, 1997 are correct, DFAS still owes Sun an interest penalty of \$440.18 on this invoice. The money is long overdue and should be paid immediately.

#### Variances in Remit Addresses.

The contract provides the "electronic payment address." It is at the Bank of America in Concord, CA. The "EFT" - electronic fund transfer - payment on this invoice was sent to this address. The invoice provides a different remit address in Los Angeles, CA. Several other payments on the same contract were sent to another remit address in Chicago, IL.



## SYBASE, INC.

We reviewed several invoices from this company but chose to focus on just two - No. 10CIO12880 and No. 38637C. In examining these transactions, we detected several serious problems as follows:

- No receiving reports
- Bogus contract number
- Mismatch between services billed and services authorized by contract
- Unauthorized payments
- Services not delivered
- Double billing
- Services delivered to Synergy, Inc.
- Services paid by DFAS and Synergy
- Payments partially refunded
- Fraud suspected
- Variance in remit addresses

### Invoices

There were at least three different versions of the first invoice - No. 10CIO12880. All are essentially the same - except early versions included \$115.50 in travel expenses and a 10 cent error in the hourly rate. The final one is dated March 6, 1997. It covers 115 hours of consulting fees by Mr. Gerald Moses from December 2, 1996 through December 20, 1996. The rate billed is \$168.42/hour. The total amount billed was \$19,368.30. It is identified as a "revised" version of an earlier invoice. It has two date stamps - March 15, 1997 and April 11, 1997.

The same invoice - No. 10CIO12880 - was submitted simultaneously to Synergy, Inc. in Washington, D.C. for payment. Only the addressees were different.

There are two versions of the second invoice - No. 38637C. One is dated August 14, 1995, and the other is dated November 16, 1995. It covers 16 hours of consulting fees by Ms. Suellen Carlin from June 1, 1995 to June 22, 1995 as well as travel expenses. The hourly rate charged is \$127.5. The total amount billed was \$2,064.25. The date stamps are: November 8, 1995 and December 11, 1995.

The heading on all the invoices cite the same contract number - No. F4010594FA789 - presumably the contract to which the bills were to be charged. Unfortunately, this contract simply does not exist. It's a phony contract number.

### Receiving Reports

The accounts payable file at the Denver center did not contain a receiving report for either invoice.

The file does contain a request for receiving report for July 29, 1997 on invoice No. 10CIO12880. It is signed by an authorized government representative, Mr. Mike Aquila. He certified that the services rendered by Mr. Moses were received and accepted on March 6, 1997. However, since the bill covered consulting services, the delivery should have been effective on the last day of service - December 20, 1996.

We met with Mr. Aquila on June 26, 1998 to ask him this question: "What was the basis for your certification?" He replied by saying: "I don't remember," and he had no records or notes. "Who is the COTR," we asked? Who is the person responsible for this service. He could not answer any of our questions. He had to call the vendor to locate the customer - who didn't exist.

We obtained a copy of the second invoice - No. 38637C - with this notation: "I certify this invoice." The signature is unreadable. There is similar notation of the other version of same invoice, but the signature is different but also unreadable.

### Invoice/Contract Mismatch

Since both invoices cite a bogus, non existent contract, DFAS charged the bills to a real Sybase contract with a very similar number - No. F4965094FA789. The real contract and the phony one share 11 numbers. The last seven digits are identical. Only four numbers are different. It would be very easy for a careless pay technician to confuse the two numbers.

The "real" Sybase contract was signed on September 4, 1994. It is signed by the contracting officer but not the vendor. It authorizes 184 hours of consulting services to be delivered by January 10, 1995. The hourly rate authorized was \$127.00 for a total award amount of \$23,460.00. The precise nature of the services to be performed were spelled out in a "scope of work" attached to the contract, but the entire contract file at Bolling AFB was destroyed. The contractor, however, was kind enough to give us a copy.

There are at least five major areas of disconnect between these invoices and the contract.

First, the contract cites fiscal year 1994 Air Force O&M appropriations for equipment as the source of funds. The work performed, by comparison, involved consulting services and not equipment, and the consulting services were provided in fiscal years 1995 and 1997 - far outside the period of performance authorized in the contract. These services were not covered by the contract. Payment for those services were not authorized by this contract.

Second, this appears to be an attempt to consume "dormant" obligations at the very end of the fiscal year. These funds should have been de-obligated and returned to the Treasury.

Third, the hourly rate charged on invoice No. 10CIO12880 - \$168.42 - exceeded the hourly rate authorized in the contract - \$127.50.

Fourth, the hourly rate charged on invoice No. 38637C - \$127.50 - matches up with the contract, but the charges for travel expenses are not authorized in the contract.

Fifth, despite the certification given by an authorized government representative, Mr. Mike Aquila, the services billed on invoice No. 10CIO12880 were not delivered on March 6, 1997 or on any other date. They were, in fact, delivered to Synergy, Inc. - private company located in Washington, D.C.

We have been unable to verify whether the services billed on invoice No. 38637C were, in fact, delivered.

#### Payments

DFAS paid the vendor \$19,462.72 for the services billed on invoice No. 10CIO12880 on September 8, 1997, including an interest penalty of \$94.42.

DFAS paid the vendor \$2,140.94 for services billed on invoice No. 38637C on August 21, 1996, including an interest penalty of \$76.69.

All the PPA computation dates - displayed on the vouchers - appear to be erroneous.

#### Mischarge or Fraud?

Was this fraud or an innocent mischarge?

#### Error Determined - Money Returned

After we starting asking questions about these invoices in March 1998, DFAS agreed to issue a "demand" letter, asking Sybase to return the money.

On May 18th, we were informed that "Sybase had researched the payment and determined that the invoice was submitted in error." The full amount for one invoice - \$19,462.72 - was returned on May 22, 1998 and credited to the correct account.

The money paid on the other invoice - No. 38637C - has not been returned.

At this point, we knew the invoices were submitted "in error," but the exact nature of the error was not yet known. But we kept asking questions.

Sybase finally admitted that the services billed on invoice No. 10CIO12880 were not provided to the government. The bill was "inadvertently" sent to DFAS instead of the correct customer. But who was the real customer? Further contact with Sybase helped to solve the mystery.

#### Double Billing

Only July 9, 1998, Sybase told us that Synergy was the customer. Contact with Synergy on July 10th confirmed this information. The project manager at Synergy, Mr. Fred Czerner, Jr., said Synergy hired Sybase and Mr. Moses to help design a "database maintenance" project on an NIH [National Institutes of Health] contract. Mr. Czerner provided a copy of Sybase's invoice. It is dated March 6, 1997 and is identified by invoice No. 10CIO12880. It is almost identical to the bill Sybase submitted to the government for the same "work." Only it is addressed to the correct customer instead of DFAS. He also provided a copy of Synergy's check that paid the bill in full. It is dated May 7, 1997.

The evidence clearly shows that Sybase simultaneously submitted identical bills for the same services to two different payment offices - DFAS and Synergy.

Mr. Czerner also reported that he warned Sybase in early 1997 that its billing for this work was improper. He was truly surprised when presented with the dates on which the government paid the bill - September 8, 1997 - and the date on which Sybase returned the money - May 22, 1998. He thought Sybase had corrected the problem right after his warning. He thinks "Sybase tried to sandwich U.S. Government work, and as a result, submitted at least 4 invoices inappropriately."

Mr. Czerner did not recognize the names of the consultants listed on the other Sybase invoice - No. 38637C. While this does not appear to be another case of a bill paid by Synergy, it could have been paid by another company for work on other government contracts. The Air Force notified us on July 15, 1998 that this invoice was "improper." The Air Force stated: "This invoice should not have been certified and no payment or interest penalty should have been paid." The money should now be returned.

#### Suspected Fraud

We suspect fraud on these two invoices for four reasons:

1) The phony contract number cited on both invoices is deceptively similar to a real one. We think this contract number was specifically designed to confuse inexperienced pay technicians at the Denver center.

2) Sybase simultaneously billed both the government and Synergy for identical work. One invoice was addressed to the correct customer - Synergy, while the other was addressed to the wrong customer - DFAS. Now, how could that happen - when the designated point of contact at Sybase is the same person - Ms. Denise Triesler at 301-897-1678?

3) Synergy warned Sybase in early 1997 that the billing was incorrect. Why didn't Sybase correct the "error" at that point?

4) The bill - invoice No. 10CIO12880 - was initially rejected because it included an unauthorized item - travel expenses (exactly like invoice No. 38639C). The bill was then revised at least twice to conform with the "wrong" contract and resubmitted. If the mistake was truly innocent as Sybase suggests, then the error should have been detected in the revision process.

#### Variance in Remit Addresses.

The contract [incorrect] provided a remit address in Bethesda, MD. Both checks were sent to an different address in San Francisco, CA. The \$19,462.72 check went to the San Francisco remit address specified on the invoice. The check for \$2,140.94 went to a San Francisco address that does not match the remit address on the invoice. There is a slight difference. It appears to have gone to a different bank "file" number - 72364 - instead of "file" No. 72417 specified on the invoice and other check.

### WASHINGTON PROFESSIONAL SYSTEMS

We reviewed several invoices from this company but focused on just one - No. 90932. In examining this transaction, we identified several problems as follows:

- No receiving report
- Impossible to reconcile invoice with contract
- Circumvention of PPA
- Tampering with invoices and date stamps
- Possible destruction of invoices
- Falsification of information in IAPS

#### Invoice

The invoice is dated April 4, 1997. It covers the delivery of equipment to update audio systems in the National Military Command Center's (NMCC) Emergency Conference Room - 3 QSC MX700 Power Amplifiers and 2 accompanying QSC MX700 service manuals. The bill totaled \$1,250.00.

The accounts payable file at Denver provides a very confusing picture about when this invoice was actually received at the center.

First, there is no date stamp on the invoice. Second, the invoice bears a fax date of "1/12/95," which DFAS says is supposed to be 1/12/98 - the date the vendor presumably faxed the invoice to DFAS. Third, handwritten notes and initials on the invoice also seem to indicate it was received on January 12, 1998. And fourth, there is a handwritten note on the invoice that suggests it was originally received on August 3, 1997.

#### Receiving Report

The accounts payable file at Denver did not contain a receiving report.

The file contains two different versions of the request for receiving report for August 4, 1997. We first examined this document during a visit to SAM in August 1997. At that point in time, it was signed by an authorized government representative, Mr. Mike Aquila, but provided no certification that the goods were received and accepted. The file at Denver in March 1998, by comparison, contained a copy of the same document we examined in August, but it included a certification that the goods were "received and accepted" on November 5, 1997. The origin of

this date is unknown. There is nothing in the file to support it. The handwriting for the November 5, 1997 entry is entirely different from Mr. Aquila's handwriting on the original document. It appears to have been "back-dated" on to the document by someone other than Mr. Aquila.

#### On-Site Inspection

We met with the customer in the NMCC, Mr. Alfredo Hernandez, on two occasions - September 8, 1997 and then again on June 1, 1998 regarding this invoice.

At the first meeting, he verified that the delivery of these items was completed on June 20, 1997. Mr. Hernandez informed us that he faxed the information to DFAS on the same day.

At the second meeting, we attempted to verify that the 3 amplifiers and manuals had, in fact, been delivered and were in inventory and accounted for today. We began by consulting the NMCC's property management system - known as APMS. The serial numbers for 3 QSC MX700 amplifiers were listed in APMS. We then checked those serial numbers against the serial numbers of the units installed in the conference room. We got a good match. However, since no serial numbers were given on either the invoice or contract, we cannot say with certainty that the components we examined were the same as those listed in the contract and invoice. Mr. Hernandez had a packing slip that included serial numbers but no prices.

The \$28.00 manuals looked like a rip off. These were not technical operating or repair manuals. They were 20-page manuals like the ones normally provided free of charge when a TV or VCR is purchased at Circuit City.

#### Invoice/Contract Mismatch

The contract became effective on December 31, 1996. It is signed by the contracting officer but not the vendor. It covers a long list of electronic equipment to update the audio equipment in the NMCC's emergency conference room. Delivery was due by February 11, 1997. The total award amount was \$5,116.30 - an amount increased by \$737.00 with a contract modification on February 7, 1997.

The quality of the copy of this contract, which was contained in the file at Denver, was so poor that it was unreadable. Given such poor copy quality, it was impossible to match the invoice with the contract. Yet this is the same document that the pay technicians at the Denver center had to consult in preparing this bill for payment.

#### Circumvention of PPA

This invoice was paid in full on February 19, 1998 - 320 days after it was submitted. The payment included an interest penalty of \$18.61.

This is a case where DFAS used falsified information to reduce the interest penalty due rather than to deny it entirely.

The PPA computation dates displayed on the voucher are as follows: Invoice receipt date - January 12, 1998; and delivery date - November 5, 1997. The invoice receipt date in this case was the driver. That was the date used to compute interest under the PPA.

Two DFAS documents prove that the invoice receipt date was fabricated to circumvent the law. It was manufactured. The DFAS documents prove that the invoice was in the center - in IAPS - 9 months before the official January 12, 1998 receipt date.

First, the invoice was listed on the request for receiving report of August 4, 1997. This means that it was in the center - and in IAPS - 5 months before official receipt date of January 12, 1998. Second, we have an IAPS report - dated October 31, 1997 - that clearly indicates that the invoice was actually received in the center on April 15, 1997. The invoice was then prepared for payment on voucher No. D700085522 dated August 26, 1997. This payment was voided for phony reasons. It was voided because there was no receiving report and no contract and \$576.52 was "over-billed." When a voucher is voided, the original voucher is then destroyed. When the voucher is destroyed, the original PPA computation dates shown on the original voucher are lost as well. It works like a laundry operation. The voiding procedure allows DFAS to officially "lose" - destroy or thrash - the original invoice - with date stamp - and create entirely new invoices with new date stamps - or request duplicate invoices from the vendor.

In all probability, the invoice receipt date of January 12, 1998 was the last time the vendor faxed a copy of this invoice to the Denver center. Contact with the vendor supports this theory. The vendor reports that the invoice was first sent to DFAS "shortly after" its April 4, 1997 date. When payment became overdue, "numerous other copies of the invoice were faxed" to DFAS. The faxes were followed by lots of phone calls.

Assuming that the invoice was actually received on April 15, 1997 and the goods were delivered on June 20, 1997, then the total interest due would be \$51.03 instead of the \$18.61 paid.

#### Remit Addresses

The remit address specified in the contract is the company's Wheaton, MD address. The check was sent to that address.

## XEROX CORPORATION

We reviewed a number of invoices from this company but focused on just three - No. 061555637, No. 579081560, and No. 579081561. In examining these transactions, we detected several problems as follows:

- Impossible to match invoice with contract
- Invoices do not give dates of service
- Unauthorized service and payment
- Overcharges
- Lease to Own Plan (LTOP) poorly defined
- Ownership dates not specified in contract or government records
- Government relies on vendor for ownership information
- Equipment could not be located

### Invoices

All three invoices cover the same model 5385 copy machine - serial No. 88Y-010241 as follows:

--No. 579081560, dated December 10, 1997, covers a monthly service charge on a lease agreement. The amount billed is \$535.55. Other than a cryptic reference to "invoice 15 of your 60 month contract," the period of service covered by the invoice is not identified.

--No. 579081561, dated December 10, 1997, covers a monthly service charge on a lease agreement. The amount billed is \$535.55. Other than a cryptic reference to "invoice 16 of your 60 month contract," the period of service covered by the invoice is not identified.

--No. 061555637, dated March 20, 1998, covers a "monthly base charge" for October 1, 1997 through December 30, 1997. The amount billed is \$1,896.00 or a charge of \$632.00 per month.

### Receiving Reports

The accounts payable file at Denver contains a form DD-250 receiving report. The DD-250 seems to match with invoice No. 061555637, but block 6 on the form, which is supposed to identify the invoice number and date, is blank. The form is signed by SSGT. Patricia J. Ebert,

who is identified as the USAF, Resource Advisor. Her signature is dated April 1, 1998. This document certifies that the quarterly maintenance charges on this machine were valid and accepted.

Certifications provided by SSGT Ebert also appear on invoices No. 579081560 and No. 579081561. These are signed and dated January 9, 1998.

### Invoice/Contract Mismatch

The contract is dated November 5, 1997 with an effective date of November 4, 1997. The contract period extends through September 30, 1998. It is signed by the contracting officer but not the vendor. The total award amount is \$38,689.32.

A contract modification was signed on January 6, 1998. It increased the total amount by \$216.00 to a new grand total of \$38,905.32. The change increased the monthly charge on the model No. 5385 copier - serial No. 88Y010241 - from \$614.00 per month to \$632.00 per month. The effective date of the increase was January 6, 1998.

The contract authorized maintenance on 9 copy machines, including 5 copiers provided under a "lease to own plan" or LTOP. Each copy machine is clearly identified in the contract by model and serial number. The monthly charges authorized for each machine are provided. Unfortunately, the contract contains no information whatsoever on the LTOP arrangement. For example, when does the government gain full ownership of these machines? The ownership date is not established in the contract. Those dates should be clearly identified in every contract.

Invoice No. 061555637 does not match with the contract. This invoice bills for unauthorized services and overcharges on monthly rates.

First, it covers the period October 1, 1997 through December 30, 1997. Since the contract did not take effect until November 4th, at least one month of the services billed lies outside of the contract period. Second, the rate charged - \$632.00 per month - is the higher rate authorized by the contract modification executed on January 5, 1998. The higher rate was not supposed to take effect until January 6, 1998. Xerox is charging the higher rate retroactively - back to October 1, 1997. The correct rate for this machine for that period of time should be \$614.00 a month. Xerox over-billed by \$54.00 on this invoice.

It is also impossible to reconcile invoices No. 579081560 and No. 579081561 with the contract without more information. First, the monthly charge on both bills appears to be correct, but the period to time covered by the invoice is not identified. Second, without the LTOP start and ending dates, it is impossible to know whether the monthly fee for the lease is valid and appropriate.

#### Overpayment

DFAS paid invoice No. 061555637 in full - \$1,896.00 - on April 20, 1998. This constituted an unauthorized payment and an overpayment. The \$632.00 paid to cover the "monthly base charge" for October 1997 was not authorized because the contract did not take effect until November 4, 1997. And the extra \$36.00 paid for the rate hike in November and December was an overpayment, since the rate increase did not go into effect until January 6, 1998.

#### On-Site Inspection

We met with SSGT Ebert, the Resource Advisor, at Bolling AFB on April 7, 1998 to locate the Xerox copiers; to verify delivery; and to determine when the government assumes ownership of the LTOP copiers.

We asked SSGT Ebert a series of questions as follows: When does the government assume full ownership of these machines? Is the ownership date recorded in another contract or in other officials documents? What are the LTOP expiration dates for each machine?

SSGT Ebert was unable to answer any of our questions.

#### --Ownership Dates

According to SSGT Ebert, the LTOP start and finish dates are not recorded in government documents. She said that when she has questions about the amount due on an invoice, period of service, or ownership dates, she calls Xerox to get the answer.

When certifying officials have to call the vendor for verification, there is no independent check. There is no independent proof of delivery. There is entirely too much room for fraud.

#### Service Verification

During our visit with SSGT Ebert, we also attempted to match the serial numbers on Xerox invoices and contract with the serial numbers on copiers in place at Bolling AFB.

SSGT Ebert's records were inaccurate and incomplete.

To assist us with the review, SSGT Ebert produced a document entitled "Copier Location." She said this was a complete, up-to-date list of all the machines under her supervision. There were 9 Xerox copiers on the list. Of those 9 machines, we got a good match on only six. Six serial numbers matched with the serial numbers on the contract. Three had serial numbers not listed on the contract. Then we attempted to match those numbers with the numbers on machines

actually in place at Bolling. We looked at 3 nearby machines. For those 3 machines, we got a good match with the contract on two, but the serial numbers on those machines did not match with the numbers on SSGT Ebert's list. The serial number on one of the machines was not found.

After this meeting SST. Ebert revised her list. A comparison of her revised list with the contract shows a perfect match - 9 for 9, but do those numbers match with the machines actually in place? We did not make a follow up check to verify the accuracy of the new list.

A failure to maintain accurate and complete records leaves these resources vulnerable to fraud and abuse. "If you don't know what you have on hand, then you don't know what is missing."

#### Variance in Remit Address

The contract provides a remit address in Philadelphia, PA. The check was sent to a Philadelphia address, but this address is entirely different from the one specified in the contract.