

Oversight Report



DEFENSE CONTRACT AUDIT AGENCY'S ROLE IN INTEGRATED PRODUCT TEAMS

Report Number D-2001-6-003

March 23, 2001

Office of the Inspector General
Department of Defense

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| Abstract In 1995, the Secretary of Defense directed that DoD use Integrated Product Teams (IPTs) as a preferred oversight and management approach in acquiring goods and services. An IPT is composed of representatives from all appropriate functional disciplines working together to facilitate decision-making. The concept was developed to streamline the acquisition process. The Defense Contract Audit Agency (DCAA) auditors support the acquisition process by participating on IPTs that address contract proposal preparation, review, negotiation, and contract award. From FY 1995 through FY 1999, the number of DCAA forward-pricing activities decreased from 16,514 to 9,834 (60 percent). However, the number of forward-pricing activities involving IPTs increased from 63 to 498 (690 percent). | | |
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Acronyms

| | |
|--------|---|
| CAM | Contract Audit Manual |
| CAS | Cost Accounting Standards |
| DCAA | Defense Contract Audit Agency |
| LMFS | Lockheed Martin Federal Systems |
| LMTAS | Lockheed Martin Tactical Aircraft Systems |
| IPT | Integrated Product Teams |
| NAVAIR | Naval Air Systems Command |



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

March 23, 2001

MEMORANDUM FOR DIRECTOR, DEFENSE CONTRACT AUDIT AGENCY

SUBJECT: Evaluation Report on Defense Contract Audit Agency's Role in Integrated Product Teams (Report No. D-2001-6-003)

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

Management comments were responsive and conformed with the requirements of DoD Directive 7650.3. No further comments are requested.

We appreciate the courtesies extended to the evaluation staff. Questions on the evaluation should be directed to Ms. Patricia A. Brannin at (703) 604-8802 (DSN 664-8802) (pbrannin@dodig.osd.mil) or Ms. Madelaine E. Fusfield at (703) 604-8739 (DSN 664-8739) (mfusfield@dodig.osd.mil). See Appendix B for the report distribution. The evaluation members are listed inside the back cover.

A handwritten signature in black ink, reading "David K. Steensma", is positioned above the typed name.

David K. Steensma
Acting Assistant Inspector General
for Auditing

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Office of the Inspector General, DoD

Report No. D-2001-6-003

March 23, 2001

(Project No. D2000-D000OA-0125, Formerly OOC-9110)

Defense Contract Audit Agency's Role in Integrated Product Teams

Executive Summary

Introduction. In 1995, the Secretary of Defense directed that DoD use Integrated Product Teams (IPTs) as a preferred oversight and management approach in acquiring goods and services. An IPT is composed of representatives from all appropriate functional disciplines working together to facilitate decision-making. The concept was developed to streamline the acquisition process. The Defense Contract Audit Agency (DCAA) auditors support the acquisition process by participating on IPTs that address contract proposal preparation, review, negotiation, and contract award. From FY 1995 through FY 1999, the number of DCAA forward-pricing activities decreased from 16,514 to 9,834 (60 percent). However, the number of forward-pricing activities involving IPTs increased from 63 to 498 (690 percent).

Objectives. The overall objective was to evaluate the role of DCAA auditors in the IPT process. Specifically, we evaluated the nature, extent, and timing of DCAA participation, and the benefits achieved from timely audits of proposal parts as the contractor submits them. We also reviewed the adequacy of management control programs relating to the area evaluated at DCAA field audit offices (Appendix A).

Results. DCAA has embraced the IPT concept and the auditors have developed good working relationships with team members while maintaining their independence. However, the requestor of audit services did not always know what specific services were required or available, and audit acknowledgments did not always explain what the auditors could or could not provide. Further, audit procedures could be improved for responding to requests for services, documenting team coordination, planning the IPT proposal reviews, and reporting the audit results. Audit file documentation frequently did not evidence auditor participation on an IPT. Budgeted and actual hours varied substantially in some instances, and standard audit programs at two offices were not adjusted to reflect the teaming arrangements. Several reports did not mention the IPT process, and one office misinterpreted the audit guidance on reporting on the results of an IPT process.

Improved information is needed for both requestors of DCAA audits and the auditors on DCAA participation in IPTs. For details of the audit results, see the Finding section of the report.

Summary of Recommendations. We recommend that the Director, Defense Contract Audit Agency, develop protocols for the use of requestors of IPT audit services. The protocols can explain auditor roles and responsibilities and what services the auditors can provide, as well as what they need from the IPT chairperson. We also recommend that the Director, Defense Contract Audit Agency, develop additional guidance for

auditor participation in IPTs. The guidance should cover acknowledgment of requests for audit support, documentation of team proceedings and conference times, and special reporting procedures.

Management Comments. The Defense Contract Audit Agency concurred in principle with the four recommendations but reserved full concurrence pending the results of an analysis of the Agency's Integrated Product Team historical performance. The analysis will be performed by a joint Headquarters/Regional team and be completed by August 2001. The Defense Contract Audit Agency fully expects that, as a result of the resources and effort that will be committed, the actions that will be taken by the end of CY 2001 will adequately address the recommendations. Refer to the Finding section of the report for a discussion of management comments on the finding and to the Management Comments section of the report for the complete text of the comments.

Evaluation Response. Management comments were generally responsive to the intent of our recommendations.

Background

On May 10, 1995, the Secretary of Defense issued a memorandum on the use of Integrated Product Teams (IPTs). The memo directed that when it makes sense, the new management concept should be used for all acquisitions. The DoD policy is to perform as many acquisition functions as possible, including oversight and review, using IPTs. The IPTs are composed of representatives from all appropriate functional disciplines. A pricing IPT is one of many IPTs that might support Defense acquisitions. A pricing IPT is assembled to review a contractor's proposal, provide information directly to the contracting officer on a real-time basis, and avoid redundant and duplicative proposal preparation procedures. The use of an IPT in pricing is designed to expedite contract awards by replacing the traditional pricing and negotiation process with a concurrent team approach.

The DoD Directive 5000.2-R, "Mandatory Procedures for Major Defense Acquisition Programs and Major Automated Information Systems," May 11, 1999, provides general guidelines for IPT procedures, roles, and responsibilities. Other DoD guidance on IPTs includes the "Rules of the Road: A Guide for Leading Successful Integrated Product Teams," 1999, the "DoD Guide to Integrated Product and Process Development," 1996, and the Defense Acquisition Deskbook.

Defense Contract Audit Agency. On January 23, 1996, Defense Contract Audit Agency (DCAA) issued a Memorandum for Regional Directors, "Audit Guidance on DCAA Participation in Integrated Product Teams and Other Streamlined Acquisition Initiatives." The guidance memorandum stated that auditors should fully participate in IPTs and related initiatives that require financial advisory services. However, to maintain audit independence, DCAA may not prepare the contractor's proposal. The DCAA role is to provide advice to the contracting officer during the proposal development on documentation requirements to support pricing information, contractor estimating techniques, any impact of outstanding estimating system deficiencies, and contractor compliance with the cost accounting standards.

The IPT process differs from other contract proposals or forward pricing audits in that the auditor participates during the proposal buildup. The contracting officer requests audit assistance before the contractor has completed the entire proposal package. Information and guidance on the auditor's role on IPTs is incorporated into the DCAA Audit Pamphlet 7641.90, Information for Contractors, which is accessible from the DCAA web site at <http://www.dcaa.mil>.

Objectives

The overall objective was to evaluate the role of DCAA auditors in IPTs. We focused on teams established to evaluate contractor proposals. Specifically, we evaluated the nature, extent, and timing of DCAA participation and the benefits achieved from timely audits of proposal parts as the contractor submits them.

We also reviewed the reporting of audit results, monetary benefits, and the adequacy of management control programs related to the area evaluated at DCAA field audit offices. (See Appendix A.)

Adequacy of Procedures for Audit Participation on Integrated Product Teams

The DCAA had embraced the IPT concept and the auditors had developed good working relationships with team members while maintaining their independence. However, the requestor of IPT audit services did not always know what services DCAA auditors could provide. Further, audit procedures for responding to requests for services, documenting team coordination, planning the IPT proposal reviews, and reporting the audit results could be improved. In 18 of 39 audit assignments, the requestor of audit services did not specify what services were required and 10 of the 18 did not address DCAA participation on an IPT. Audit acknowledgments were responsive to the requests but did not explain what services the auditors could or could not provide. Of 39 audit assignments, 9 did not adequately document auditor participation on an IPT. Budgeted and actual hours varied substantially in some instances, and auditors at two field audit offices had not adjusted the standard audit programs to reflect the teaming arrangements. Of the 39 reports that resulted from the audit assignments, 12 did not mention the IPT process, and one office misinterpreted the audit guidance for reporting on the results of the team review.

Improved information is needed for both requestors of DCAA audits and the auditors on participation in IPTs. DCAA also needs to improve its acknowledgment of requests, documentation of meetings, and reporting.

DCAA Participation on Integrated Teams

Increased Use of IPTs. DCAA participation on IPTs has increased significantly since the Secretary of Defense directed the use of this management approach to acquisition. DCAA has performed fewer conventional forward-pricing reviews as the requests for audit participation in acquisition teaming arrangements has increased. For example, at Northrop Grumman Corporation, the DCAA effort spent on IPTs has increased from about 11 percent of all price proposal reviews in 1997 to 50 percent of all proposal reviews in 1999. At Lockheed Martin Tactical Aircraft Systems (LMTAS), auditors spent 28 percent of proposal review hours on IPTs in FY 1997. As of the second quarter of FY 2000, IPT hours comprised 52 percent of all price proposal review activity. Agency-wide, DCAA has experienced an increase in requests for auditor participation in IPTs even though proposal reviews have declined overall, as shown in the following Table.

Summary of DCAA Forward-Pricing Activity

(\$ in Billions)

| Activity | FY 95 | | FY 97 | | FY 99 | |
|-----------------------|--------|----------|--------|--------|-------|--------|
| | No. | \$ | No. | \$ | No. | \$ |
| Price Proposals | 8,418 | \$140.7 | 4,571 | \$56.7 | 3,148 | \$41.2 |
| IPTs | 63 | 0.3 | 402 | 14.2 | 498 | 19.2 |
| Specified Elements | 1,224 | 20.7 | 775 | 7.7 | 553 | 4.5 |
| Agreed Upon Proc. | 3,295 | | 3,983 | | 3,199 | |
| Rate Agreements | 2,795 | | 2,313 | | 2,141 | |
| Other Forward Pricing | 719 | | 440 | | 295 | |
| Totals | 16,514 | \$ 161.7 | 12,484 | \$78.6 | 9,834 | \$64.9 |

The participation in IPTs has resulted in increased audit staff time to complete the forward-pricing/contract proposal audits. Since 1996, DCAA has spent an average of three times as many hours completing a forward-pricing review while participating in an IPT than the number of hours spent on a conventional price proposal review. For example, in FY 1996 DCAA spent an average 63.1 hours on a price proposal review and 184.5 hours on an IPT. In FY 2000, the average price proposal review took 72.9 hours whereas the average IPT consumed 242.4 hours. Although the increased time may be attributed to more time spent in team meetings and other factors, we were unable to determine exactly how the additional time was spent because of insufficient documentation in the audit files.

We spoke to 8 auditors who had completed 28 of the 39 audit assignments evaluated. With one exception, they believed the IPT process was helpful. However, they recognized that the process required more time to complete an audit than conventional audits. The benefits are derived from better understanding of program requirements and access to technical information. Based on limited inquiries at four program offices, the program offices responded that the time to award a contract had decreased considerably. However, only two of the four program offices could provide specific examples to illustrate reduced acquisition time. Other benefits included improved communications and better understanding of program requirements. All four program offices agreed that the greatest difficulty is the availability of team members.

DCAA has included guidance on participation on IPTs in its Contract Audit Manual and provided information on audit participation in IPTs in the pamphlet on "Information for Contractors," which can be accessed from the DCAA web site. However, audit guidance can be improved to specifically cover the following:

- Clarification of audit services requested;
- Improved documentation of auditor role;

-
- Improved audit planning; and
 - Reporting.

DCAA should issue information to the acquisition community that outlines its policies and procedures relating to auditor participation in IPTs and should clarify to its auditors what is and what is not participation in an IPT.

Clarification of IPT Audit Services

Documentation of Early Agreement on Audit Services. In 18 of 39 audit assignments reviewed, the procurement office request for audit services did not specify what type of audit services would be needed, and 10 of the 18 requests did not specify that the requested support involved participation in an IPT. In 4 of the 18 audit assignments, a request for specific services was received after the team had reviewed the complete proposal but before an audit report was issued. The following two examples illustrate the wide range of differences observed in documentation to indicate agreement on requested audit services:

- In one example at Northrop Grumman, the only record of an audit request was a note on a telephone message from the procurement office. DCAA received no request for audit services. The only source of program office information on expected audit services was a weekly activity report prepared by DCAA.
- At LMTAS, the Air Force provided an example of a useful request that summarized agreements and discussions held at a pre-proposal conference, confirming oral agreements reached with DCAA and other Government personnel to perform in-process audits of material quotes.

Because requestors may not know the scope of audit services that will be needed early in the acquisition process, DCAA must define what services are available and what the potential constraints for audit participation may be for each audit. Although other participants on a team may sign an agreement to outline tasks to be performed and clarify expectations, DCAA Contract Audit Manual (CAM) chapter 1-808, Memorandum of Agreement, states that the auditing standard on independence precludes DCAA from entering into an agreement on audit scope. However, there should be a clear understanding of the audit services that are to be provided. Instead of signing an agreement, the auditor may satisfy the customer's needs by communicating to the team leader in writing the auditor's expected role on the team. Therefore, DCAA should consider developing a pro forma acknowledgment letter to explain what services auditors can or cannot provide, similar to the illustration in CAM Figure 1-8-1, Notification Letter to Contractor, which addresses DCAA participation on process action teams. The notification letter outlines conditions for auditor participation.

Non-IPT Requests for Audit Services. Not all requests for early participation in the acquisition process may have involved the support of an IPT. In two cases at Northrop Grumman and two cases at Lockheed Martin Federal Systems

(LMFS), neither the documentation in the audit file nor the information provided to the requestor appeared to support classifying the audit as an IPT assignment. However, when DCAA was requested to participate early in a proposal review, the audit offices established the assignments as IPTs in anticipation of above average audit effort being required.

At LMFS, Naval Air Systems Command (NAVAIR) requested early DCAA participation in the Alpha Acquisition process, the NAVAIR term for the IPT process. However, the two assignments we evaluated covered minor dollar amounts (\$1.5 and \$5.3 million, respectively), and less than 100 hours were spent in each case. The services DCAA rendered did not appear to require more interaction with contracting parties and technical specialists than would be expected during a conventional audit. In one case at Northrop Grumman, the Program Office asked DCAA to provide rates and factors only. A second request merely asked DCAA for early support to streamline the technical evaluation/audit process. In each case, the auditor provided rate information based on existing forward pricing rates and spent 90 and 79 hours, respectively.

The “Rules of the Road” guide stresses some significant operating principles, including the need for an IPT charter that should contain:

- a clear mission statement, to include the specific purpose and objective of the IPT;
- identification of the output product and the customer;
- the time frame by which the product is to be produced; and
- the IPT membership, including all the cross-functional disciplines necessary to achieve the IPT objective.

The guidebook cautions that IPTs are not intended to solve every problem and should be distinguished from meetings. IPTs are focused on building successful acquisition programs, but not all issues for resolution or assigned actions require convening an IPT.

Auditors need to know whether a formal acquisition IPT with a charter has been established before concluding that requests to participate in early meetings constitute participation in an IPT. Because teaming arrangements are increasing, and the time taken to participate in IPTs is more than expended on conventional audits, the DCAA management information system needs to be able to reflect differences between IPT assignments and other forward-pricing activity. DCAA issued a Memorandum for Regional Directors on Audit Management Guidance for Integrated Product Team (IPT) Assignments, 98-OWD-076(R), August 10, 1998, to clarify previous audit guidance on IPTs and provide attributes for an IPT. However, if the work involves limited technical assistance, or provision of readily available information, the assignment should not be classified as participation in an IPT.

Documentation of the Audit Role

Independence is a key concern of auditors participating in IPTs. The DCAA auditor must comply with the Generally Accepted Government Auditing Standards as implemented by DCAA in CAM, chapter 2-203, Independence. The CAM guidance requires the auditor to maintain an independent attitude and appearance in all matters related to the audit work. To safeguard auditor independence during IPT participation, CAM chapter 1-806, Auditor's Role on DoD IPTs and Related Streamlined Acquisition Initiatives, instructs the auditor not to assist the contractor in actually preparing the contractor's proposal. Contractor management should approve proposal parts before the auditor begins the audit. DCAA should not review unapproved, in-process estimates.

Overall, the DCAA auditors participating in IPTs had sufficient training and experience to recognize when to withdraw from a teaming arrangement or to declare a proposal not ready for their review. Therefore, nothing came to our attention to indicate that auditors were unable to maintain their independence. However, documentation of team coordination and information exchange could be improved.

Audit File Documentation on Team Coordination. Of the 39 audit assignments reviewed, 12 assignments at Northrop Grumman, 14 assignments at LMTAS, and 4 assignments at LMFS included adequate examples of documentation of exchanges with team participants. In some instances the documentation was excellent and facilitated an understanding of the purpose and scope of the team efforts. The conference notes were particularly important when the initial requests for audit support did not clearly explain what was expected of the auditors.

However, the remaining nine audit assignments did not provide sufficient information to show the extent or nature of teaming arrangements. Inadequate documentation in two of the four assignments at FS indicated that auditor participation in an IPT was probably limited and that the assignments may have been misclassified. Of 21 assignments at TAS, 7 should have included more information on the extent of teaming that had occurred. For example, the requests for audit services in six of the seven assignments did not address auditor participation on IPTs. Auditors participating in IPTs need to document their involvement to distinguish the IPT process from routine meetings and conferences that auditors participate in as part of regular audits. The documentation should also safeguard them from any appearance of impairments to auditor independence during the IPT process and keep supervisory auditors informed of team activities.

To facilitate DCAA supervision of the auditor's work on the team and to ensure that auditors participating in teaming arrangements maintain their independence, auditors should document key meetings and exchanges of information in the standard workpaper sections designated for that purpose, or where appropriate. CAM chapter 4, General Audit Requirements, provides guidance on audit coordination with contract administration personnel, contractor internal and external auditors, and conferences with the contractor. None of the sections

addresses the special concerns inherent in teaming arrangements, and the CAM guidance on the auditor's role on IPTs does not emphasize the need for documentation of team meetings and discussions. The nature and extent of documentation on coordination varied in the audit files.

DoD Procedures for IPTs. DoD program offices had different procedures for implementing DoD policy on the use of IPTs in acquisition. The F-16 program office, LMTAS, DCMA, and DCAA had jointly developed a detailed process, Span Time of Acquisition Reduction, or "STAR," and had provided an extensive briefing to the auditors on the process that they found highly informative and useful. The B-2 office had developed a description for its "B-2 Paradigm" process. The F-22 program office responded that no procedures were available for its "One Pass" process, and auditors were less familiar with either of these procedures or those developed by NAVAIR to explain its Alpha Acquisition method. Although DoD guidance recommends that the program leader develop a charter for each IPT, auditors were generally unaware that such a document might be available to explain the specific acquisition objectives. Of the 39 assignments evaluated, only one included a copy of the IPT charter.

Although auditors typically participated in initial meetings at which they obtained timeline charts that identified the phases most crucial to auditor involvement, they stated that more familiarity with the overall process would be useful. One supervisory auditor expressed a need for more up front information about the acquisition processes used, believing it would greatly facilitate planning of audit resource allocation.

Audit Planning

Although audit coverage appeared adequate, audit planning, including risk assessments and the recording of budgeted and actual audit hours expended could be improved at two of the three offices visited.

Preliminary Planning and Risk Assessments. The 39 audit assignments included preliminary audit programs and risk assessments. However, one office did not incorporate the planning considerations in CAM chapter 3-300, Internal Control Audit Planning Summary, and 25 of 33 assignments at 2 locations did not discuss contractor compliance with the cost accounting standards.

Resident Audit Office at Northrop Grumman Corporation. Audit planning was adequate and risk assessments were very good for the 12 audit assignments evaluated at the Northrop Grumman resident audit office. The Northrop Grumman audit office benefited from special regional guidance for implementing CAM guidance. The regional guidance provided instruction as to how risk assessments should be developed; what risk factor considerations should be used; and how low, moderate, or high risk should be assessed. The audit guidance required the auditor to provide source and explanation for all assessments. The result was that the auditor was directed to exercise judgment and not merely post the outcome of other audits.

Resident Audit Office at LMTAS. In 9 of 21 audit assignments covering large procurement dollars over \$5 million, the auditors used standard audit programs intended for small procurements under \$5 million dollars. The DCAA also found this condition during a FY 1999 quality assurance review of price proposals. Based on that review, DCAA developed new proposal review guidance effective February 4, 2000, that should correct the condition.

Planning of Cost Accounting Standards Compliance Testing. None of the three audit offices had documented the need for tests of contractor compliance with Cost Accounting Standards (CAS) 401 and 402 in either the risk assessment workpaper section or the detailed audit programs. CAM chapter 8-305.2, Compliance Review Testing, requires that testing of the standards be planned during the performance of proposal evaluations or incurred cost audits. In response to a recommendation in Report No. PO 99-6-001, January 11, 1999, "DCAA Audits of Contractor Compliance with Cost Accounting Standards," DCAA updated standard forward pricing audit programs in 1998 to include a risk assessment that should be performed to determine whether testing is required during the subject audit. However, none of the audits we reviewed that were completed in FYs 1999 or 2000 used the updated audit programs. DCAA also identified this condition during the FY 1999 quality assurance review. Because the new Audit Planning and Performance System incorporates preliminary audit procedures for considering CAS implications for proposals exceeding \$5 million, we are making no further recommendation at this time.

Budgeted versus Actual Hours. At two locations, the actual hours recorded in the audit program did not identify time spent in teaming activities, such as meetings and conferences. Without an accurate recording of how audit effort was spent, the offices had no baseline for budgeting new effort.

At Northrop Grumman Corporation, audit programs were adequate and procedures were identified to teaming efforts with hours spread among broad tasks performed. However, it was not possible to determine how many of the hours were spent in performing audit analysis, engaging in teaming activities, or providing financial advisory services, if any. In two assignments the actual hours recorded in the audit assignment also varied from the actual hours recorded in the management information system. In one of the two assignments, no actual hours were noted in the assignment against the 410 budgeted hours, but the management information system showed 754 hours spent. In the other, the audit assignment showed 199 hours incurred compared to the 651 recorded in the management information system.

The audit programs in the 21 assignments at Lockheed Martin Corporation did not allocate hours to individual review procedures, and the programs were not tailored to account for the time spent in teaming arrangements or other non-audit tasks. Only the total hours spent reviewing a cost element were recorded. One entry merely showed 380 hours to review material costs. Audit programs were not adjusted to explain special effort involved in IPT work. Budgeted hours in 3 of the 21 assignments were considerably lower than the actual hours incurred.

The CAM chapter 3-103, The Audit Program, instructs auditors to tailor the standard audit program based on documented risk assessments and the specific audit objectives. CAM chapter 3-103.h requires the auditor to reference each audit step to the working paper(s) where the step was accomplished and to record the actual hours expended on each step or group of steps. Further, the actual hours recorded in the audit program should agree with the time reported in the management information system. Given the apparent significant increase in time spent on an IPT review versus a traditional proposal review, the accurate recording of hours is needed for effective management.

Audit Report Procedures

An audit report issued as a result of auditor participation on an IPT should mention that fact and provide some information about the IPT process used, for example, the extent of DCAA participation and access to technical information. Before preparing the audit report, the auditor should coordinate with the contracting officer to determine any special reporting requirements. The DCAA audit guidance contains no special reporting provisions for proposal reviews performed as part of an IPT process. Based on services requested, CAM chapter 1-806 directs the auditors to CAM chapter 10-300, Audit Reports on Price Proposals, for reporting on either a comprehensive audit, a review of specified cost elements only, or the application of agreed-upon procedures.

Reporting on the IPT Process. Of 39 audit reports reviewed, 12 did not mention the IPT process. Nine of the 12 reports were issued from the LMTAS resident audit office and the remaining 3 from the Northrop Grumman residency. The remaining 27 reports made some reference to the IPT process but did not explain to what extent that affected the audit. For example, because auditors participated in the pricing review before the contractor had completed the proposal package, they may or may not have had a comprehensive bill of material from which to draw a statistical sample. Further, although the DCAA audit reports follow a standard format that includes specific audit areas that must be addressed, the reference to the IPT process was included in different sections in different reports. The 6 reports at LMFS referred to the Alpha contracting process or an IPT in the “Subject” section or the “Explanatory Notes.” CAM reporting guidance does not address the need for comments on the IPT process, and the audit offices used different procedures.

Audit Opinion. The limited CAM guidance for reporting the results of an IPT proposal review may have been misinterpreted at one field audit office. At the LMFS field office, all the reports issued as part of an IPT process covered only “agreed-upon procedures” and expressed no opinion as prescribed in CAM chapter 10-306.4, Results of Application of Agreed-upon Procedures. The DCAA auditors believed it was inappropriate to express an audit opinion based on reviews performed as part of an IPT and, therefore, chose the reporting procedures for applications of agreed-upon procedures. These reviews are evaluations of limited information, such as verification of current labor or overhead rates, verification of estimating techniques, or application of certain attest procedures. However, at least three of the six assignments showed specific requests for DCAA audits of specified cost element with no restrictions on audit scope.

CAM chapter 1-806(f) advises the auditor to follow the appropriate reporting procedures in CAM chapter 10 for each specific review. The guidance also states that the IPT reports should express an opinion, although the opinion will vary depending on the services performed. If no restrictions were imposed on the scope of review of a particular proposal element, DCAA guidance would require a report on specified cost element with an audit opinion expressed.

Summary

Because of the expanding role of IPTs and the resources that are needed to support the IPTs, DCAA needs to clarify its guidance to its auditors and the information to its clients on the use of auditors in the IPT process. DCAA should enhance its CAM guidance and provide a readily available description of protocols for the program officials to use in requesting audit services. The protocols should be based on the existing guidance and information in the CAM and the audit pamphlet "Information for Contractors," supplemented with best practices and lessons learned.

Management Comments on the Finding and Evaluation Response

Management Comments. The DCAA response to the draft report requested clarification on a few statements. On the increased use of IPTs, DCAA stated that the audit files contained some support to indicate that meetings had occurred. On non-IPT requests for audit services, DCAA also disagreed with one of the four cases identified as not having adequate documentation to support classifying the audit as an IPT. The DCAA also believed a statement to be inaccurate that none of the three audit offices had documented the need for tests of contractor compliance with CAS 401 and 402 in either the risk assessment workpaper section or the detailed audit programs. According to DCAA, the IPT audit assignments evaluated at one office used agreed-upon-procedures that typically would not call for CAS compliance testing. In addition, DCAA noted that the SPO, LMTAS, DCMA, and DCAA jointly developed the STAR process.

Evaluation Response. Documentation was not sufficient to record how much time the auditor spent in meetings. An e-mail or single line item listing of a meeting does not provide information on what occurred at the meeting or prove that the auditor attended. We also questioned the practice of routinely establishing an IPT merely because the requester used the term "IPT." Where the request for audit support is limited to rates and factors or specified cost elements, coordination with the requestor is advisable to ensure that the scope of review will require extensive audit participation in meetings or financial advisory services other than providing existing information. We believed the practice at one audit office to limit the scope of all IPT effort to agreed-upon-procedures was inappropriate in part because it resulted in CAS compliance

testing not being performed or even considered. As a result of DCAA comments, we modified the report to identify the joint development of the STAR process.

Recommendations

We recommend that the Director, Defense Contract Audit Agency:

- 1. Develop protocols for use of program officials on auditor participation on acquisition teams. The protocols could explain the auditor's role and responsibilities, and what services the auditor can provide, as well as what the auditor needs from the Integrated Product Team chair.**
- 2. Develop a pro forma acknowledgment letter to be issued in response to non-specific requests for audit support to a team. The pro forma request should describe audit services that can be provided and identify audit constraints.**
- 3. Issue guidance to emphasize the need to record the nature of information exchanged during team meetings and to record conference time in the audit program.**
- 4. Develop reporting procedures that address the special circumstances that should be considered when an audit is completed as a result of a team process. Audit guidance should require that the audit report discuss the audit participation in an Integrated Product Team evaluation.**

Management Comments. The DCAA concurred in principle with the recommendations but reserved full concurrence pending the results of an analysis of the Agency's Integrated Product Team historical performance. The analysis will be performed by a joint Headquarters/Regional team and completed by August 2001. The DCAA expected that the actions to be taken by the end of Calendar Year 2001 would adequately address the recommendations.

Evaluation Response. The proposed actions are generally responsive to the intent of our recommendations.

Appendix A. Evaluation Process

Scope and Methodology

Work Performed. We visited three DCAA field audit offices that participated in IPTs at Lockheed Martin Tactical Aircraft Systems, Northrop Grumman Corporation, and Lockheed Martin Federal Systems. We also met and interviewed Administrative Contracting Officers at those locations.

- To determine the nature, extent, and adequacy of DCAA participation in IPTs, we reviewed 39 forward-pricing audits completed during FY 1997 through the date of our field visits during the second quarter of FY 2000.
- To obtain information on reductions in acquisition cycle times, we requested data from the B-2, F-16, and F-22 Special Program Offices and the Naval Air Systems Command.
- To obtain support for information gathered at field audit offices, we also met with the resident Administrative Contracting Officers participating in the IPTs at LMTAS and NGC.

Deleted Scope. We deleted the announced objective to evaluate the audit contribution to the overall procurement cycle-time reduction. Initial information gathered indicated that the data would not be available. We also deleted the objective to review management control programs at the DoD Military Department buying commands because it was outside the scope of the primary evaluation.

Use of Computer-Processed Data. We relied on computer-processed data from the DCAA Agency Management Information System to identify field audit offices participating in IPTs. Although we did not perform a formal reliability assessment of the computer processed data, we determined that the assignment numbers, dollars examined, and questioned costs for the selected audit assignments generally agreed with the computer-processed data. We did not find errors that would preclude use of the data to meet the evaluation objectives or that would change our report conclusions.

Universe and Sample. Using the DCAA Agency Management Information System, we requested information on all audits performed during a 3-year period ending September 30, 1999. Based on the results, we judgmentally selected three field audit offices that had a large number of audit assignments sufficient for an evaluation and that covered major procurement programs. At LMTAS, we reviewed all but one of 22 IPT assignments completed during FYs 1998 and 1999. We did not evaluate one assignment because it was similar to several other assignments included in the sample. At Northrop Grumman and

LMFS, we evaluated all IPT assignments completed during FYs 1997 through the date of the field visits in March 2000, 12 and 6 audit assignments, respectively.

Evaluation Type, Dates, and Standards. We performed this economy and efficiency evaluation from January 2000 through November 2000 according to standards implemented by the Inspector General, DoD. The project was suspended from August to November to complete higher priority work. Accordingly, we included tests of management controls at field audit offices related to auditor participation in the IPT process.

Contacts During the Evaluation. We visited or contacted individuals within DoD. Further details are available upon request.

Management Control Program Review

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, and DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996, require DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of controls.

Scope of the Review of the Management Control Program. We reviewed the DCAA management controls over forward-pricing audits performed as part of an IPT process. Specifically, we reviewed management controls over audit programs, documentation of coordination with team members, and audit reporting.

Adequacy of Management Controls. DCAA management controls were adequate in that we identified no material management control weaknesses.

Prior Coverage

No prior coverage has been conducted on the subject during the last 5 years.

Appendix B. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition, Technology, and Logistics
Director, Defense Procurement
Under Secretary of Defense (Comptroller/Chief Financial Officer)

Department of the Army

Auditor General, Department of the Army

Department of the Navy

Naval Inspector General

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and Comptroller)

Other Defense Organizations

Director, Defense Contract Audit Agency
Director, Defense Contract Management Agency

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Defense Contract Audit Agency Comments



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

IN REPLY REFER TO

PQA 225.4[0OC-9110]

February 27, 2001

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

SUBJECT: Response to Draft DoDIG Evaluation Report on DCAA's Role in Integrated Product
Teams (Project No. D2000-D000OA-0125, formerly 0OC-9110)

Our comments on the subject report and its recommendations follow:

A. Clarifications. In general, we think the report fairly presents the audit work that was performed and the results of that work. There are, however, a few statements in the report that appear to warrant further clarification. The statements are presented below, followed by our clarifying remarks:

1. Draft Report Page 4, Paragraph 1:

The participation in IPTs has resulted in increased audit staff time to complete the forward-pricing/contract proposal audits. Since 1996, DCAA has spent an average of three times as many hours completing a forward-pricing review while participating in an IPT than the number of hours spent on a conventional price proposal review. For example, in FY 1996 DCAA spent an average 63.1 hours on a price proposal review and 184.5 hours on an IPT. In FY 2000, the average price proposal review took 72.9 hours whereas the average IPT consumed 242.4 hours. Although the increased time may be attributed to more time spent in team meetings and other factors, we were unable to determine exactly how the additional time was spent because of insufficient documentation in the audit files.

DCAA – The data from our Quality Assurance (QA) organization's FY 1999 PCIE-based review supports that a good part of the increase in hours spent on IPTs was indeed due to the auditors attendance in meetings. Your data, we believe, further support this. The auditors were typically *encouraged* by the customer to become full-team members and attend the majority of IPT meetings, even though it appeared that many of the meetings covered non-audit related topics. The QA reviewers also generally found insufficient documentation in the audit files to support the time spent at the meetings. More often than not, however, there was

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documentation supporting the fact that there were meetings held, although sometimes, it was just an e-mail notice or a single line item on a table listing the meetings.

2. Draft Report Page 6:

Non-IPT Requests for Audit Services. Not all requests for early participation in the acquisition process may have involved the support of an IPT. In two cases at Northrop Grumman and two cases at Lockheed Martin Federal Systems (LMFS), neither the documentation in the audit file nor the information provided to the requestor appeared to support classifying the audit as an IPT assignment. However, when DCAA was requested to participate early in a proposal review, the audit offices established the assignments as IPTs in anticipation of above average audit effort being required.

DCAA – One of the LMFS cases cited as not being a legitimate IPT audit set-up appears to be incorrect or is certainly explainable. The subject of the request for assignment 98H2200104 states "IPT" and an IPT Code 220 audit assignment was set-up even though the requestor limited the review to subcontract costs and rates. Tailoring DCAA's effort to an *agreed-upon procedure* or *part of a proposal* review as part of an IPT is entirely appropriate and the auditor in such cases is guided to set-up the audit as a Code 220 assignment.

3. Draft Report Page 9:

Planning of Cost Accounting Standards Compliance Testing. None of the three audit offices had documented the need for tests of contractor compliance with Cost Accounting Standards (CAS) 401 and 402 in either the risk assessment workpaper section or the detailed audit programs.

DCAA – We believe that the statement and data for at least one of the audit offices – the National Branch Office -- is inaccurate. The Code 220 audit assignments that were evaluated at the Branch were all *agreed upon procedures* reviews, which typically would not call for the planned testing of contractor CAS compliance.

4. Draft Report Page 8:

DoD Procedures for IPTs. DoD program offices had different procedures for implementing DoD policy on the use of IPTs in acquisition. The F-16 program office had developed a detailed process, Span Time of Acquisition Reduction, or "STAR," and had provided an extensive briefing to the auditors on the process that they found highly informative and useful. ...

Page 5

Page 8

Page 7 revised

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DCAA – The Field Audit Office cognizant of the F-16 program has informed us that the STAR process was actually jointly developed by the SPO, Lockheed Martin Aeronautics-Fort Worth, DCMA, and DCAA.

B. Recommendations. The draft report on page 11 recommends that the Director of DCAA:

1. Develop protocols for use of program officials on auditor participation on acquisition teams. The protocols could explain the auditor's role and responsibilities, and what services the auditor can provide, as well as what the auditor needs from the Integrated Product Team chair.
2. Develop a pro forma acknowledgment letter to be issued in response to non-specific requests for audit support to a team. The pro forma request should describe audit services that can be provided and identify audit constraints.
3. Issue guidance to emphasize the need to record the nature of information exchanged during team meetings and to record conference time in the audit program.
4. Develop reporting procedures that address the special circumstances that should be considered when an audit is completed as a result of a team process. Audit guidance should require that the audit report discuss the audit participation in an Integrated Product Team evaluation.

DCAA

Recommendations 1, 2, and 3:

We concur in principle to Recommendations 1, 2, and 3. The recommendations appear reasonable and on point in light of the evaluators' reported findings and what was reported to DCAA's management as a result of the QA organization's FY 1999 PCIE-based review. In fact, DCAA's Executive Steering Committee (ESC) believes that the results of both reviews, together with the management feedback generated by the reviews, have indicated that there are potentially significant opportunities for improving the Agency's IPT-related processes and services at this time.

Prior to committing to specific action, the ESC further believes that more specific data and analysis is needed on some of the problems that were surfaced (e.g., the expended hours, number of meetings attended, and audit set-up and coverage problems). To obtain the additional data and analysis, the ESC established Action Item E00-12-5 in December 2000. The Action Item calls for DCAA Headquarters (Operations & Policy) to "form a joint Headquarters/Regional team to specifically analyze the Agency's Code 22000 historical performance between and within regions to identify risk factors, customer requests, and different practices that influence individual proposal productivity within the 22000 strata." May 2001 was originally established as the completion date for the additional review effort.

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The regional part of the review effort, however, will not begin until after the Action Item is further discussed at the March 2001 ESC meeting. For this reason, while not yet officially changed, we now believe that the project completion date will slip to August 2001.

On the basis of the actions taken by the ESC noted above, we are reserving our full concurrence to the recommendations at this time. We fully expect, however, that as a result of the resources and effort we are committing this year to the IPT area, the actions that we will take by the end of CY 2001 will adequately address Recommendations 1, 2, and 3 above.

Recommendation 4:

Based on discussions held with the IG Evaluators after issuance of the draft report, we also concur in principle with what we now believe to be the intent behind the IG's Recommendation 4, restated below,.

4. Develop reporting procedures that address the special circumstances that should be considered when an audit is completed as a result of a team process. Audit guidance should require that the audit report discuss the audit participation in an Integrated Product Team evaluation.

It is very important to DCAA that its auditors perform their work in the independent manner called for by the *second general Government Auditing Standard*. It is also important that they consistently use language in their audit reports that clearly reflects the independent nature of the audit work performed. This is especially true with regard to audits that are performed in situations where the auditor is also a member of an integrated product team (IPT). For this reason, DCAA's reporting guidance intentionally does not recognize nor address any "special circumstances" that need to be considered when an audit is completed as part of an IPT. In short, although the IPT process is a team process, DCAA's principal role still involves the issuance of an independent audit report. Such a process does not and should not create "special circumstances" that impact how the independent DCAA auditor reports his/her results.

Having made the above point, the IG evaluation, its draft report, and recommendation 4 therein, have brought to our attention the likely need to improve our audit reporting guidance related to IPTs. It appears that some new guidance is needed to further ensure that the reporting language does not unintentionally lead the reader to believe that something less than a fully independent audit was performed. On page 10 of the draft report, the IG evaluators note 27 DCAA price proposal audit reports that include references to the IPTs in which the DCAA auditors were members. Further review of these reports, coupled with the results of the Agency's review of its Code 22000 audits now underway, should provide the supporting data needed to appropriately add to and/or revise our reporting guidance.

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Questions regarding this memorandum should be directed to Mr. Henry Simpkins, Quality Assurance Division at (703) 767-2250.

/s/ Robert DiMucci
/for/ Lawrence P. Uhlfelder
Assistant Director
Policy and Plans

Evaluation Team Members

This report was prepared by the Deputy Assistant Inspector General for Audit Policy and Oversight, Office of the Assistant Inspector General for Auditing, DoD.

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