

Master Document – Audit Program

Activity Code 11010	Billing System and Related Internal Controls
Version 7.0, dated June 2004	
B-1	Planning Considerations
Purpose and Scope	
The major objectives of this audit are to:	
<ul style="list-style-type: none"> • Evaluate the adequacy of and the contractor’s compliance with the billing system internal controls. 	
<ul style="list-style-type: none"> • Obtain a sufficient understanding of the contractor’s billing system and related internal controls (including both manual and computerized activities) to plan related audit effort. This requires that the auditor assess the adequacy of the contractor’s policies and procedures, whether they have been implemented, and if they are working and being monitored effectively. 	
<ul style="list-style-type: none"> • Document the understanding of the billing system internal controls in working papers and permanent files. 	
<ul style="list-style-type: none"> • Assess control risk as a basis to identify factors relevant to the design of substantive tests. 	
<ul style="list-style-type: none"> • Report on the understanding of the billing system internal controls and assessment of control risk and the adequacy of the system for Government contracts. 	
<p>This audit is limited to the examination of the billing system and related internal controls for major contractors, non-major contractors where the system is considered significant, and other contractors with substantial firm-fixed price contracts. Only those controls directly related to the contractor’s billing system, as defined below, will be audited under this assignment. Controls for interrelated audit concerns regarding the adequacy of the contractor’s other major systems (i.e., budget and planning, estimating, etc.) will be audited under separate assignments. While the controls for these areas are not part of this audit, the results of all audits of these interrelated controls must be considered in forming an overall audit conclusion on the billing system internal controls. The results of this audit should be commented on in reports on related audit areas.</p>	
<p>When performing an update or follow-up examination, the steps below should be adjusted and tailored accordingly. To the extent possible, prior audit effort should be used as a basis for validating the contractor’s internal controls.</p>	
<p>Before beginning this examination, the auditor should be alert for internal control evaluations performed by the contractor or its external auditors relating to this audit area. In those cases where internal control evaluations have been performed, the auditor should follow guidance contained in CAM 4-1000, Relying Upon the Work of Others.</p>	
<p>Before performing any examination of internal controls, the auditor should determine that the system contemplated for examination is material to the Government. Once it is determined that the system is material to the Government, the auditor should reassess the materiality of each</p>	

Master Document – Audit Program

<p>section in the internal control audit before performing any audit steps in that section. The scope of any audit depends on individual circumstances. The auditor is expected to exercise professional judgment, considering vulnerability and materiality, in deciding the scope of audit to be performed.</p>
<p>The use of computers of all kinds in a contractor’s accounting and management systems is so pervasive it is unlikely that any audit of them could be performed adequately without an examination of the internal controls over their automated aspects. Therefore, the auditor should become familiar with guidance contained in the Information System (IS) Auditing Knowledge Base that is found on DCAA’s Intranet, prior to the beginning of this audit. In addition, in some instances, the assistance of IT specialists may be required to adequately evaluate the automated aspects of the internal controls. In these cases, auditors should coordinate, through their supervisory auditor, to contact their regional office to obtain the necessary expertise.</p>
<p>The internal control matrix (see Internal Control Matrix – Billing System and Related Internal Controls), showing the interrelationships among the control objectives, control activities, and audit procedures used in this audit program, is located in APPS under “Other Audit Guidance.” The control objectives and the audit procedures have been fully integrated into this audit; therefore, the matrix is not needed unless it is desirable to see the associated control activities and the interrelationships in a matrix format.</p>
<p>The following documents are available in APPS under “Other Audit Guidance” to assist the auditor in preparing the vulnerability assessment, working papers, and letters required for this audit. They should be tailored to fit the circumstances.</p>
<ul style="list-style-type: none">• Direct Billing Letters.doc
<ul style="list-style-type: none">• Proforma Notification to Payment Office.doc
<ul style="list-style-type: none">• Proforma Request for Assist Audit
Definitions
<ul style="list-style-type: none">• Contract Overpayments. Overpayments are payments that the contractor receives that are in excess of billed amounts. Overpayments may also result from differences between recorded and billed costs. Major causes of overpayments include: (i) weaknesses in contractor internal controls; (ii) contract administration adjustments; and (iii) paying office errors.
<ul style="list-style-type: none">• Accounting for Progress Payment Liquidations. The Government liquidates (recoups) progress payment amounts previously provided to contractors by deducting these amounts from the payment requested on the appropriate contractor delivery invoice. Consequently, the contractor should have procedures for recording, in its accounting records, the net delivery invoice amount that reflects the reduction of the delivery invoice amount by any prior progress payments requested by the contractor and paid by the Government.
<ul style="list-style-type: none">• Contract Administration Adjustments. Contract administration adjustments include payments the contractor received in accordance with contract provisions, which need to be reduced because of subsequent events or actions. Contract administration adjustments

Master Document – Audit Program

may result from contract administration related actions, such as:
<ul style="list-style-type: none"> • progress payment adjustments due to a contract loss position;
<ul style="list-style-type: none"> • changes in contract billing prices, liquidation rates, and foreign exchange rates;
<ul style="list-style-type: none"> • quarterly limitation of payment adjustments;
<ul style="list-style-type: none"> • Government withholds as a result of contract performance problems; and
<ul style="list-style-type: none"> • settlement of final indirect rates, Cost Accounting Standard noncompliances, or postaward audits.
<ul style="list-style-type: none"> • Demand Letters. Letters issued by the paying office or contracting officer demanding payment of specified amounts by the contractor. The demand letter notifies the contractor that amounts not paid within 30 days of the demand letter shall bear interest.
<ul style="list-style-type: none"> • Offsets. An offset is a reduction applied to an invoice submitted to the paying office as a means of resolving payment issues such as overpayments, contract administration adjustments, and paying office/contractor errors.
<ul style="list-style-type: none"> • Refunds. Checks submitted to the Government during a specific time period.
References
1. CAM 3-300 Internal Control Audit Planning Summary (ICAPS)
2. CAM 5-100 Obtaining an Understanding of a Contractor’s Internal Controls and Assessing Control Risk
3. CAM 5-1100 Audit of Billing System Internal Controls
4. CAM 6-203 Credits and Refunds on Cost-Type Contracts
5. CAM 6-705 Interim Cost-Reimbursable Billings
6. CAM 6-900, Notice of Cost Suspensions and Disapprovals Under Cost Reimbursable Contracts
7. CAM 6-1000, Responsibilities for Processing and Approval of Interim and Completion Cost-Reimbursable Vouchers
8. CAM 14-200, Audit of Progress Payments

B-1	Preliminary Steps	W/P Reference
	Version 7.0, dated June 2004	
1.	Research and Planning	
	a. Become familiar with applicable sections of CAM 5-1100, and any	

Master Document – Audit Program

recent relevant Headquarters guidance not incorporated in the CAM located on the DCAA’s intranet under DCAA Audit/Administrative Guidance.	
b. Perform the following steps using the permanent file:	
(1) Review prior billing system audit working paper package.	
(2) Identify any billing system deficiency reports issued (review ICRS database, as applicable). Document the results of (1) and (2) on W/P B-2.	
(3) Determine if there are any reported deficiencies in the other internal control system audits that impact the scope of this billing system audit (review ICRS database, as applicable). Document on W/P B-2. The results of the Control Environment and Overall Accounting Controls examination, if any, should also be evaluated and documented, in detail, under Control Environment, Section C-1, Step 1 of the W/Ps and under Information and Communications, Section E-1, Step 1. The results of the IT Systems General Internal Controls examination, if any, should also be evaluated and documented in detail under Information and Communications, Section E-1, Step 1.	
(4) Identify the sources for the detailed policies, procedures, charts, etc., called for in steps (a) through (d) below. Document the sources of data by listing the data, its source, and any changes since the last system audit.	
(a) Contractor’s written policies and procedures and billing system manual.	
(b) Organization charts depicting the functional areas responsible for developing and processing billing related data.	
(c) Billing system flowcharts providing a pictorial overview of all manual and computerized processing steps.	
(d) Information systems documentation:	
(i) Pertinent record layouts of files created and/or used during the processing of billing system related transactions.	
(ii) Database table definitions.	
(iii) Source documents.	
(iv) Information on the conversion of documents to computer media.	

Master Document – Audit Program

(v) Subsidiary or master files affected by the system.	
(vi) Relevant reports, journals, and ledgers produced in the flow of information to the billing system reports.	
(5) Review audit lead sheets.	
(6) Review other related audits, for example:	
(a) Review results of prior examinations of paid vouchers (11050).	
(b) Review results of prior examinations of progress payments (175XX).	
(c) Review results of prior examinations of contract overpayments (17310).	
(d) Review results of prior examination of contractor compliance with billing instructions (17390).	
(e) Review and summarize the impact of suspected irregular conduct (SIC), and CAS noncompliances, if applicable.	
(7) Consider the impact of the contractor’s financial condition on the billing system. (Refer to prior financial capability assessments or audits – 176XX).	
c. In planning and performing the examination, consider the fraud risk indicators specific to the audit. The principal sources for the applicable fraud risk indicators are:	
<ul style="list-style-type: none"> • Handbook on Fraud Indicators for Contract Auditors, Section II.4 (IGDH 7600.3, APO March 31, 1993) located at www.dodig.osd.mil/PUBS/index.html, and 	
<ul style="list-style-type: none"> • CAM Figure 4-7-3. 	
Document in working paper B any identified fraud risk indicators and your response/actions to the identified risks (either individually, or in combination). This should be done at the planning stage of the audit as well as during the audit if risk indicators are disclosed. If no risk indicators are identified, document this in working paper B.	
d. Obtain from the contractor a schedule of total dollars processed through the billing system for the past twelve months (or most recently completed fiscal year) and summarize by total dollars and dollars by Government flexibly priced contracts and fixed price contracts in order to determine the materiality of the billing system. Update ICAPS as applicable.	
e. Discuss the planned evaluation of the billing system internal	

Master Document – Audit Program

<p>controls with the administrative contracting officer (ACO) and the contractor's major procurement activities to identify, understand, and document any concerns they may have of areas which should be evaluated. The auditor should reassure the ACO and procurement activities that DCAA billing system audits can satisfy customer requirements and eliminate the need for submittal of excessive contractor documentation with interim vouchers. In addition, determine if the ACO wants us to perform specific audit services to support the ACO's responsibilities under FAR 32.503-5, Administration of Progress Payments, or other guidance.</p>	
<p>f. FAOs that have cognizance of contractors with significant classified contracts should coordinate with the Field Detachment to determine the DCAA office responsible for identifying and reviewing billings and overpayments on classified contracts. This coordination should be documented in the working papers. FAOs should also coordinate with the Field Detachment on any significant billing system issues, including overpayments found on classified contracts during prior period reviews.</p>	
<p>g. Close coordination is required at FAOs cognizant of a shared services location and the FAOs cognizant of the segments serviced by the shared services. Document the objectives and procedures to be performed at the shared services location and the segment level. Request assist audits, as applicable.</p>	
<p>h. Determine the extent and results of the contractor's self-governance activities, internal and external audits, and coordinated audits related to the billing system.</p>	
<p>(1) Request the contractor provide a list of completed internal and external audits and determine if any are related to the billing system.</p>	
<p>(2) If applicable, coordinate with the CAC or corporate office auditors to determine if any internal control weaknesses that might impact the billing system were identified in management's internal control report or the independent auditor's attestation on management's assertion included in the annual report filed with the SEC.</p>	
<p>(3) In those cases where internal or external audits have been performed, the auditor should follow the guidance contained in CAM 4-1000, Relying Upon the Work of Others. Document your preliminary evaluation and its impact on the scope of this examination. The evaluation of internal audit working papers is documented in detail under Management Reviews in Section G-1, step 3.</p>	
<p>i. Determine the need for technical assistance, if any, and document</p>	

Master Document – Audit Program

your consideration on working paper B-3.	
2. Entrance Conference and Preparation	
a. Prepare a written memorandum to the contractor to arrange for an entrance conference, covering the areas highlighted in CAM 4-302 and any specific data or pertinent information not yet provided.	
b. Conduct an entrance conference as outlined in CAM 4-302, with particular emphasis on:	
(1) Requesting the contractor to provide, if applicable, a system orientation briefing or a demonstration of the billing system transaction flow including data input, data processing, data output, and related internal controls. Document under Information and Communications, Section E-1, Step 3.	
(2) Determining any changes in the billing process since the last examination.	
(3) Discussing the contractor's risk assessment process. Overall understanding of contractor's processes will be documented under Contractor Risk Assessment Section D-1.	
(4) Discussing the contractor's monitoring process to ensure that established manual and computerized controls are functioning as intended. Document under Monitoring, Section F-1.	
(5) Identifying the contractor's billing system procedures and internal controls that assure timely identification and resolution of contract overpayments including the following:	
(a) <u>Comparison of Billed and Paid Amounts Received.</u> Request the contractor to provide copies of and explanations, as needed, of the following:	
(i) its procedures for comparing amounts billed to amounts received at the invoice level, its accounting procedures for applying progress payment liquidations on delivery invoices and for recording the net delivery invoice amount in the accounts receivable records for comparison to amounts received, and the process for resolving payment variances (including notifying the Government or prime contractor, if applicable, when overpayments are identified and returning the overpayments);	
(ii) a listing of all current outstanding payment variances on prime contracts and subcontracts (including variances due to liquidation differences); and	

Master Document – Audit Program

<p>(iii) the current accounts receivable and accounts payable aging reports.</p>	
<p>(b) <u>Reconciliation of Recorded to Billed Costs</u>. Request the contractor to provide a copy of such a reconciliation and the following:</p>	
<p>(i) its procedures for performing the periodic reconciliation of recorded to billed costs;</p>	
<p>(ii) a schedule of the reconciliation of recorded and billed costs for all significant contracts and subcontracts (including physically complete contracts awaiting closeout with no recent billing activity); and</p>	
<p>(iii) a listing of all physically complete contracts awaiting closeout.</p>	
<p>(c) <u>Contract Administration Adjustments</u>. Request a listing of contract administration adjustments processed over the last 12 months. Request the contractor to explain its procedures for processing contract administration adjustments impacting billings.</p>	
<p>(d) <u>Demand Letters</u>. Request the contractor to provide a listing of demand letters processed over the last 12 months. Request the contractor to explain its procedures for processing Government demand letters for payments.</p>	
<p>(e) <u>Subcontractor Billings</u>. Request the contractor to explain its procedures for monitoring subcontractor billings and to provide a list of the top 3-5 subcontracts, including subcontract values. Based on the contractor’s explanation and a review of the subcontractor listing, determine if assist audits are required. See Step I-1, 7.</p>	
<p>(f) <u>Offsets</u>. Request a listing of all offsets processed over the last 12 months. Request the contractor to explain its procedures for processing offsets.</p>	
<p>(g) <u>Refunds</u>. Request the contractor to provide a listing of all refunds processed over the last 12 months. Request the contractor to explain its procedures for processing refunds to the Government.</p>	
<p>(6) Discussing any identified weaknesses which may have been previously reported and related follow-up actions taken.</p>	
<p>(7) Identifying any contracts with requirements to submit excessive documentation with interim vouchers such as: travel/ODC reports, labor detail, time cards, or receipts for</p>	

Master Document – Audit Program

travel/ODC.	
3. Other Preliminary Steps	
a. Determine the degree a computerized system is used in the billing system process.	
b. Perform a high level cursory assessment to determine if the following exist:	
(1) A functional billing organization with defined organizational responsibilities.	
(2) A written description of the work flow in the billing process.	
(3) Policies and procedures for effectively controlling the billing process.	
(4) Ensure that contractors who have contracts requiring registration in the Central Contractor Registration (CCR) database (i.e., contracts that contain the clauses at FAR 52.232-33, DFARS 252.204-7004 or NASA FAR Supplement 1804.7402) have adequate controls to maintain its registration in the CCR database on an annual basis. (CAM 5-1103c)	
c. Verify and document that the contractor meets the following direct billing program criteria:	
(1) Submits final year-end indirect incurred cost proposals in accordance with FAR 52.216-7(d)(2)(i) (within 6 months after the expiration of the contractor’s fiscal year). Reasonable extensions may be granted, in writing, by the contracting officer.	
(2) Submits final vouchers in accordance with FAR 52.216-7(d)(5) (within 120 days after settlement of the final annual incurred cost rates for all years of a physically complete contract) or a previously agreed-to plan to get current.	
4. Initial Risk Assessment	
Using the information obtained in steps 1, 2, and 3, prepare an initial risk assessment (W/P B) to determine the initial scope of the examination.	

C-1	Control Environment	W/P Reference
	Version 7.0, dated June 2004	
	The control environment sets the tone of an organization, influencing the control consciousness of its people. It is the foundation for all other	

Master Document – Audit Program

components of internal control, providing discipline and structure. The auditor should obtain a sufficient understanding of the control environment to determine the impact that it may have on the overall effectiveness of the billing system internal controls.	
1. Evaluate the most recently completed ICAPS for the Control Environment and Overall Accounting Controls for the rationale behind any moderate or high-risk assessment ratings and determine the impact, if any, on the effectiveness of the billing system internal controls on the control environment.	
2. If an examination of the control environment has not been recently performed, evaluate all documented prior audit experience with the contractor, including permanent files, relevant audit reports and working papers, suspected irregular conduct (SIC) referrals and discussions with prior auditors. Obtain an understanding of the following factors:	
a. Integrity and ethical values.	
b. Commitment to competence.	
c. Board of directors and/or audit committee participation.	
d. Management’s philosophy and operating style.	
e. Organizational structure.	
f. Assignment of authority and responsibility.	
g. Human resource policies and procedures.	
3. Document your overall understanding of the control environment and the impact that it has on the nature and extent of testing of each control objective (W/Ps G, H and I).	

D-1	Contractor Risk Assessment	W/P Reference
Version 7.0, dated June 2004		
The auditor should develop a sufficient understanding of the risk assessment process currently employed by the contractor in terms of its identification, analysis, and management of risks relevant to the preparation of contract cost data and the generation of contract billings.		
1. Meet with responsible personnel to obtain an overview of the various risk factors considered by management.		
2. Once the various risk factors are identified, obtain an understanding of how management identifies the risks, estimates the significance of risks, assesses the likelihood of their occurrence, and relates them to		

Master Document – Audit Program

contract reporting.	
3. If applicable, obtain an overview of any plans, programs, or actions management may initiate to address specific risks. Keep in mind that, depending on the nature of specific risks, management may elect to accept a given risk due to costs or other considerations.	
4. Document your overall understanding of the contractor’s risk assessment practices and the impact that it has on the nature and extent of testing of each control objective (W/Ps G, H and I).	

E-1	Information and Communications	W/P Reference
Version 7.0, dated June 2004		
Information and communication processes consist of the methods and records established to record, process, summarize, and report contract cost data. The auditor should develop a sufficient understanding of the contractor’s information and communication processes (relevant to contract cost data) to identify significant classes of transactions and how they are initiated, processed, controlled, and reported.		
1.	Since the accounting and information systems are integral components of information and communication processes, review the most recently completed ICAPS for the Control Environment and Overall Accounting Controls and the IT Systems General Internal Controls for the rationale behind any moderate or high-risk assessment ratings and determine the potential impact, if any, on the effectiveness of the billing system internal controls on information and communications.	
2.	Evaluate relevant permanent files, prior audit working papers, and any prior contractor demonstrations of its billing system information and communication processes.	
3.	Determine if the contractor has made changes to the information and communication processes in its billing system since the last demonstration. Evaluate the changes. If no prior systems demonstration was performed, have the contractor provide one. Contractor representatives providing the demonstration should possess a detailed knowledge of the billing system. The demonstration provides the auditor an opportunity to query contractor personnel regarding internal controls and how they are monitored. The auditor should ensure that the demonstration addresses the internal control activities outlined in CAM 5-1100.	
4.	The contractor should include appropriate manual and computerized controls in its information processing that check for accuracy, completeness, and proper authorization of billing related transactions.	

Master Document – Audit Program

<p>Have the contractor identify and demonstrate controls related to each of the areas listed in a through e below. Compare the contractor disclosed controls with the generic access control listing contained in the referenced CAM section and identify any controls not incorporated in the application. Verify the existence and adequacy of the contractor disclosed controls. Discuss any apparent deficiencies with the contractor.</p>	
<p>a. Access Controls (CAM 5-1406.1)</p>	
<p>b. Data Input Controls (CAM 5-1406.2)</p>	
<p>c. Processing Controls (CAM 5-1406.3)</p>	
<p>d. Error Correction and Submission (CAM 5-1406.4)</p>	
<p>e. Output Controls (CAM 5-1406.5)</p>	
<p>5. Selectively trace billed amounts through the billing system to validate your understanding of the information and communication processes in the billing system. Discrepancies between your understanding and the contractor’s demonstration should be resolved prior to completing the remainder of this examination.</p>	
<p>6. Document your confirmed understanding of the contractor’s billing system information and communication processes and obtain a written confirmation from the contractor indicating that they agree with this understanding. This documentation will typically take the form of system flowcharts or narrative descriptions and can be prepared by the auditor or consist of documentation prepared by the contractor (see CAM 5-106). Based on your understanding of the contractor’s billing system information and communication processes, document the impact that it will have on the nature and extent of testing of each control objective (W/Ps G, H and I).</p>	

F-1	Monitoring	W/P Reference
Version 7.0, dated June 2004		
<p>Monitoring is a process that assesses the quality of internal control performance over time. It involves assessing the design and operation of controls on a timely basis and taking necessary corrective actions. The auditor should develop a sufficient understanding of the contractor’s ongoing monitoring activities and/or separate evaluations related to the billing system internal controls.</p>		
<p>1. Determine if ongoing monitoring procedures are incorporated into the normal recurring activities of the contractor’s organization. These procedures should include regular management and supervisory</p>		

Master Document – Audit Program

activities.	
2. Where applicable, determine the extent of internal audit involvement in performing monitoring functions through separate evaluations.	
3. Determine and document the extent of monitoring activities being performed by external parties.	
4. Document your overall understanding of the monitoring activity being performed at the contractor’s location and the impact it will have on the nature and extent of testing of each control objective (W/Ps G, H and I).	

G-1	Management Reviews	W/P Reference
Version 7.0, dated June 2004		
<p>The auditor should obtain an understanding of the contractor's control activities for this control objective. A detailed understanding of the control activities is essential to the assessment of control risk. Billing system primary control objectives and examples of control activities, as they relate to U.S. Government contracts, are provided in the internal control matrix on the DCAA intranet under audit programs - Internal Control Matrix - Billing System and Related Internal Controls. The audit procedures for this control objective are also included in the internal control matrix. If the auditor determines that relevant internal control activities do not exist, or that the effort to perform tests is not justified, no control testing need be performed, and control risk will be assessed as high.</p>		
<p>1. In planning the following audit procedures to understand the contractor’s control activities, the auditor should recognize the other components of internal control and their impact on the nature and extent of testing to be performed. Document the impact of the internal control components on the nature and extent of testing on this control objective. Internal control components are as follows:</p>		
<ul style="list-style-type: none"> • Control environment 		
<ul style="list-style-type: none"> • Contractor risk assessment 		
<ul style="list-style-type: none"> • Information and communications 		
<ul style="list-style-type: none"> • Monitoring 		
<p>2. Verify that periodic reviews of contractor’s policies and procedures are conducted to ensure that:</p>		
<ul style="list-style-type: none"> a. Policies and procedures are compliant with applicable Federal regulations and contract terms. 		

Master Document – Audit Program

b. Policies and procedures have been implemented and are working effectively.	
c. Follow-up actions are taken on recommendations resulting from management reviews.	
3. Evaluate the contractor’s record of completed internal audits and its current internal audit plan to determine if the billing system is being subjected to periodic reviews in accordance with established policies and procedures.	
4. Identify and selectively evaluate documentary evidence and the frequency of the contractor's management reviews to determine whether the scope of such reviews are appropriate, the conclusions sound, and appropriate follow-up actions were taken.	
5. Identify any reviews which may have an impact on this examination, and evaluate the reports and supporting working papers to determine if any system deficiencies were noted, and the extent to which we can rely on the work performed (see CAM 4-1000).	

H-1	Policies and Procedures	W/P Reference
	Version 7.0, dated June 2004	
	The auditor should obtain an understanding of the contractor's control activities for this control objective. A detailed understanding of control activities is essential to the assessment of control risk. Billing system primary control objectives and examples of control activities, as they relate to U.S. Government contracts, are provided in the internal control matrix on the DCAA intranet under audit programs - Internal Control Matrix – Billing System and Related Internal Controls. The audit procedures for this control objective are also included in the internal control matrix. If the auditor determines that relevant internal control activities do not exist, or that the effort to perform tests is not justified, no control testing need be performed, and control risk will be assessed as high.	
	1. In planning the following audit procedures to understand the contractor’s control activities, the auditor should recognize the other components of internal control and their impact on the nature and extent of testing to be performed. Document the impact of the internal control components on the nature and extent of testing on this control objective. Internal control components are as follows:	
	<ul style="list-style-type: none"> • Control environment 	
	<ul style="list-style-type: none"> • Contractor risk assessment 	

Master Document – Audit Program

<ul style="list-style-type: none"> • Information and communications 	
<ul style="list-style-type: none"> • Monitoring 	
2. Evaluate the contractor's written policies and procedures and assess their adequacy in the following areas:	
a. Training of employees involved in the preparation of billing requests. Verify that:	
(1) Policies, procedures, and course materials are updated to comply with revisions to company policies, and Government rules and regulations.	
(2) Training includes relevant topics, such as billing procedures, briefing of contracts, applicable FAR and contract requirements, etc.	
b. Briefing of contracts, including responsibility, frequency and adequacy of briefing, to identify and document billing requirements, including all contract modifications, withholds, special provisions, etc. and update of the briefs accordingly.	
c. Management review of billings prior to submission.	
d. Evaluating the adequacy of subcontractors' accounting and billing systems prior to providing the subcontractors with interim financing.	
e. Monitoring the adequacy of subcontractors' accounting and billing systems and identifying and resolving subcontractor overpayments/underpayments, contract administration adjustments, offsets, and refunds. Ensure that contractor procedures:	
(1) Provide for obtaining documentation on the adequacy of the subcontractor accounting and billing systems, including obtaining documentation that the subcontractors provide timely notification to the prime contractor of any overpayments/underpayments,	
(2) Provide for obtaining, on a periodic basis, the subcontractors' reconciliation of billed and paid amounts on the subcontract,	
(3) Require the contractor to immediately notify the subcontractor(s) of any contract administration adjustment impacting the subcontractor(s)' billings and that refunds or offsets are processed within 30 days, and	
(4) Require the prime contractor to timely adjust its billings or submit refunds to the Government for identified subcontractor overpayments that have been included in billings to the	

Master Document – Audit Program

Government, contract administration adjustments, offsets, and refunds.	
f. Processing timely contract administration adjustments. Ensure that the contractor:	
(1) Maintains a schedule of contract administration adjustments,	
(2) Computes adjustments accurately, and	
(3) Reflects the impact of contract administration adjustments in billings or refunds within 30 days of the date of the administration adjustment.	
g. Processing Government demand letters for payment. Ensure that procedures:	
(1) Appropriately identify demand letters,	
(2) Require refunds or offsets to be submitted within 30 days of the date of the demand letter, and	
(3) Require submission of documentation to the paying office within 30 days of the date of the demand letter if the amount in the demand letter is disputed.	
h. Assessing the adequacy for processing timely offsets. Ensure that the contractor's procedures:	
(1) Require significant offsets of overpayments and contract administration adjustments to be made only after notification to, and instruction from, the contracting officer and paying office (and the contractor maintains adequate documentation of this coordination),	
(2) Require processing of approved offsets on a timely basis, usually within 30 days of identification of the overpayment or contract administration adjustment,	
(3) Require processing of offsets only on the same contract where the overpayment or contract administration adjustment occurred,	
(4) Allow processing of offsets only on valid invoices submitted to the paying office,	
(5) Do not allow the contract to remain in an overpaid status after the offset is processed, and	
(6) Require adequate accounting records to be maintained to show all offsets at the invoice level and the overpayment/underpayment status for all in-process and physically completed contracts.	

Master Document – Audit Program

<p>i. Reconciliation of billing system data to the cost accounting records. If applicable, ensure that practices used to accumulate and bill costs are consistent with practices used to estimate contract costs (CAS 401/FAR 31.201-1 and 31.203(d)) and that costs accumulated and billed are allowable in accordance with FAR 31.</p>	
<p>j. Reconciliation of recorded costs to billed costs and submitting timely credit billings and refunds where billed costs exceed incurred costs due to subsequent cost reductions to the contract. Ensure that the contractor:</p>	
<p>(1) Reconciles recorded and billed costs on a periodic basis for both in-process and physically complete (but not closed) contracts, and</p>	
<p>(2) Submits credit billings and refunds timely when billed costs exceed recorded costs.</p>	
<p>k. Adjustment of billings to reflect appropriate interim, year-end and final indirect rates and direct costs including an evaluation of subcontractors' billings to determine if they are also making interim, year-end, and final billing rate adjustments.</p>	
<p>l. Exclusion of the following nonbillable items from billings:</p>	
<p>(1) Accrued costs of direct materials and subcontract costs that the contractor (i) did not pay in accordance with the terms and conditions of the subcontract or invoice and (ii) ordinarily will not pay prior to submission of the contractor's next payment request to the Government.</p>	
<p>(2) Accrued costs that the contractor is delinquent in paying in the ordinary course of business.</p>	
<p>(3) Accrued costs of pensions, post retirement benefits, and profit-sharing or employee stock-ownership plans that have not been paid at least quarterly (within 30 days after the end of the quarter).</p>	
<p>(4) Costs of progress payments made to subcontractors on terms less favorable to the Government than the progress payment clause contained in the prime contract. In cases where the costs of subcontract progress payments are included in billings to the U.S. Government, ensure that the contractor has procedures to protect against overpayment and losses. These procedures should include the monitoring of performance and expected profitability of the subcontractors and reducing or suspending subcontractor progress payments as necessary.</p>	
<p>m. Estimates of costs attributed to items delivered/invoiced.</p>	

Master Document – Audit Program

n. Prompt notification to the Government that adjustments of billings may be required for potential loss contracts for that portion of the costs attributable to the loss.	
o. Title to Government assets whose costs are billed to the U.S. Government.	
p. Use of the most current estimate to complete to prepare the billings.	
q. All changes to the billing system and related software are validated and briefed to the Government prior to implementation.	
r. Maintenance of cumulative allowable cost records required for the accurate and timely preparation of interim and final vouchers.	
s. Monitoring the timely preparation and submittal of final vouchers.	
t. Comparisons of amounts received to amounts billed for each invoice and follow-up with the paying office if amounts differ. If amounts received are greater than amounts billed, the difference should be immediately remitted to the paying office [FAR 52.232-25(d), -26(c), -27(l)]. Verify procedures to identify and document the contractor's process for resolving overpayments within 30 days after the overpayment is made.	
u. Ensure that on contracts with progress payments, the appropriate progress payment liquidation rate is applied when the delivery invoice is recorded in the contractor's accounting records. Contractors should have procedures to:	
(1) Brief the contract to identify the appropriate liquidation rate,	
(2) Apply the appropriate liquidation rate against the delivery invoices and record the net amount in the accounts receivable records (for comparison to amounts received),	
(3) Identify payment variances as a result of differences in application of liquidation rates between the paying office and the contractor,	
(4) Research payment variances to determine if overpayments exist, and	
(5) Immediately refund overpayments due to liquidation errors and coordinate with paying office and resolve within 30 to 60 days (refund or offset on next billing) if overpayments are due to timing differences.	
v. Reduction of billed amounts on delivery invoices for previously received progress payments.	
w. Withholding of fixed fees for cost reimbursement and T & M/labor	

Master Document – Audit Program

hour contracts in accordance with contract terms, if applicable.	
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I-1	Implementation of Policies and Procedures	W/P Reference
Version 7.0, dated June 2004		
<p>The auditor should obtain an understanding of the contractor's control activities for this control objective. A detailed understanding of the control activities is essential to the assessment of control risk. Billing system primary control objectives and examples of control activities, as they relate to U.S. Government contracts, are provided in the internal control matrix on the DCAA intranet under audit programs - Internal Control Matrix – Billing System and Related Internal Controls. The audit procedures for this control objective are also included in the internal control matrix. If the auditor determines that relevant internal control activities do not exist, or that the effort to perform tests is not justified, no control testing need be performed, and control risk will be assessed as high.</p>		
<p>1. In planning the following audit procedures to understand the contractor’s control activities, the auditor should recognize the other components of internal control and their impact on the nature and extent of testing to be performed. Document the impact of the internal control components on the nature and extent of testing on this control objective. Internal control components are as follows:</p>		
<ul style="list-style-type: none"> • Control environment 		
<ul style="list-style-type: none"> • Contractor risk assessment 		
<ul style="list-style-type: none"> • Information and communications 		
<ul style="list-style-type: none"> • Monitoring 		
<p>2. The auditor should ensure that policies and procedures are executed to assure only billable costs/prices/fees applicable to U.S. Government contracts are included in billings in accordance with applicable regulations and contract terms, by performing the following steps:</p>		
<p>a. Interview billing personnel to determine whether they are familiar with, have access to, and actually refer to the written policies and procedures.</p>		
<p>b. Test to determine if the policies and procedures are being followed by:</p>		
<p>(1) Observation of the billing process, and</p>		
<p>(2) Inspection of selected billing records and documentation.</p>		

Master Document – Audit Program

<p>c. Selectively evaluate evidence that employees responsible for preparing billing requests have been trained in applicable billing policies and procedures. For example, check training records, course materials, and attendance sheets; interview employees; etc.</p>	
<p>d. Selectively compare the contractor's contract briefings to the applicable contracts and billings to determine if the contracts were adequately briefed and that they reflect unique contract requirements in their billing.</p>	
<p>e. Selectively evaluate evidence that management reviewed and approved billings. For example, verify management approval signatures, etc.</p>	
<p>f. Selectively verify that the adequacy of subcontractors' accounting and billing systems are assessed prior to providing the subcontractors with interim financing.</p>	
<p>g. Select 3 to 5 significant subcontracts to ensure that the prime contractor is verifying its subcontractor's procedures for identifying and resolving overpayments, contract administration adjustments, offsets and refunds are being complied with. If these procedures are not being addressed by the prime contractor, request assist audits from the cognizant FAOs.</p>	
<p>(1) Assist audits are generally required on subcontracts where the prime contractor does not have visibility over payment variances in the subcontractor accounting records. Assist audit requests should identify the subcontractor name and provide information on the subcontracts to be included in the request, e.g., subcontract number, period of performance, subcontract price, and subcontract type. Use pro forma request for assist audit in APPS.</p>	
<p>(2) Immediately notify the paying office, with a copy to the contracting officer, of any subcontractor overpayment, contract administration adjustment, offset or refund that the contractor has not reflected in billings or refunds to the paying office. Use the pro forma notification to payment office memo located in APPS.</p>	
<p>h. Verify that the contractor's schedule of contract administration adjustments is complete by performing the following processes:</p>	
<p>(1) Selectively review contract briefings on major contracts to identify required contract administration adjustments, such as, quarterly limitation of payments,</p>	
<p>(2) Review contract modifications on major contracts for prior 12 months to identify contract administration adjustments and</p>	

Master Document – Audit Program

verify that they were included on the schedule, and	
(3) Obtain the contracting officer’s comments on the completeness and accuracy of the schedule for major contracts selected in Step h(1) above.	
i. Select and review a sample of significant contract administration adjustments administered by the contractor to determine:	
(1) The reason(s) for the adjustment,	
(2) If the adjustment was accurately recorded, and	
(3) That a refund or offset was processed within 30 days of the date of the adjustment. Notify the paying office, with a copy to the contracting officer, of any outstanding contract administration adjustment over 30 days old where a refund or offset has not been processed. Use the pro forma notification to payment office memo located in APPS.	
j. Test completeness of the contractor’s list of demand letters. Coordinate with the regional Task Force member to obtain a listing of demand letters for the contractor (the request should include contractor CAGE code).	
k. Select and review a sample of significant demand letters issued during the last 12 months to determine:	
(1) the reason(s) for the demand letter,	
(2) that the contractor has processed a refund or offset or disputed the debt in a timely manner (within 30 to 60 days), and	
(3) that the contractor maintains adequate documentation for its position on any disputed debt. Immediately notify the paying office, with a copy to the contracting officer, of any demand letter that is over 30 days and has not been properly refunded, offset, or disputed. Also notify the paying office, with a copy to the contracting officer of any disputed debt not supported by the contractor or where documentation has not been submitted to the paying office. Use the pro forma notification to the payment office in APPS.	
l. Review a sample of significant offsets to determine if they meet the criteria for allowable offsets discussed in H-1, step h above.	
m. The offsets should have already been identified during the review of billed and paid amounts, reconciliation of recorded and billed costs, contract administration adjustments, demand letters, and subcontract billings. If additional items are found during the review of offsets, request the contractor to explain why the items were not included in the data provided under Preliminary Audit Section B-1, Step 2b(5)(f) for each of the areas and perform	

Master Document – Audit Program

<p>additional audit work, if necessary. Immediately notify the paying office, with a copy to the contracting officer, of any offsets that do not meet the above criteria, using the pro forma notification to the payment office in APPS.</p>	
<p>n. Verify the completeness of the list of refunds (obtained in Preliminary Audit Section B-1, Step 2b(5)(g)) to the Government for the last 12 months by selectively comparing the list to copies of checks issued to the Government.</p>	
<p>o. Select a sample of significant refunds to:</p>	
<p>(1) determine the reason(s) for the refund(s) and the adequacy of the documentation related to the refund, and</p>	
<p>(2) determine whether the refunds were processed in a timely manner, i.e., 30-60 days after the overpayment occurred.</p>	
<p>p. The refunds should have already been identified during the review of billed and paid amounts, reconciliation of recorded and billed costs, contract administration adjustments, demand letters, and subcontract billings. If additional items are found during the review of refunds, request the contractor to explain why the items were not included in the data provided for the applicable area and perform additional audit work, if necessary, to verify that the data discussed in Schedule I-1, Steps h through n above are complete.</p>	
<p>q. Selectively evaluate billing system and related software changes to determine if they were validated and briefed to the Government prior to implementation.</p>	
<p>r. Selectively evaluate contractor comparisons of amounts received to amounts billed for each invoice and determine, when the amount differs, if appropriate notifications were made to the paying office (especially for overpayments). Determine if the paying office’s requested actions were complied with.</p>	
<p>s. Selectively compare contractor reconciliations of billing system data to the cost accounting records. If applicable, ensure that practices used to accumulate and bill costs are consistent with practices used to estimate contract costs (CAS 401 and FAR 31.201-1 and 31.203(d)) and that the costs accumulated and billed are allowable in accordance with FAR 31.</p>	
<p>t. Review the contractor’s reconciliation of recorded to billed costs to verify it includes all significant contracts (including all open physically completed contracts with no recent billing activity). Compare the contracts included in the contractor’s reconciliation schedule to a verified listing of in-process and physically complete contracts. Determine that the calculation of recorded costs (for this comparison purpose) is based on acceptable indirect rates (see</p>	

Master Document – Audit Program

<p>CAM 6-705.1). For any contract where billed costs exceed recorded costs, request the contractor to process credit billings and refunds. If the contractor does not make adjustment to billings to reflect allowable recorded costs, consider issuing a DCAA Form 1. For other than cost type contracts (or if Form 1 is not feasible), notify the contracting officer and paying office of the overpayment using the proforma notification to payment office memo located in APPS.</p>	
<p>u. Verify that the contractor promptly adjusts billings to reflect appropriate interim revisions, year-end and final indirect rates and directs costs. Ensure that subcontractors make comparable adjustments in their billings.</p>	
<p>v. Review the accuracy and completeness of the contractor’s listing of outstanding overpayments, if any.</p>	
<p>(1) Selectively review the contractor’s comparisons of amounts received to amounts billed and other contractor documentation to determine if the list of payment variances is accurate and complete.</p>	
<p>(2) Review outstanding amounts on the aged accounts receivable and accounts payable listings to ensure these amounts are appropriately included on the list of outstanding overpayments.</p>	
<p>(3) Determine if the contractor’s listing of overpayments includes all payment variances as a result of delivery invoice liquidation differences between the contractor and paying office. Review the contractor’s accounting procedures for progress payment liquidations to verify that all outstanding variances have been identified. If liquidation differences are not identified, develop audit steps to identify the differences.</p>	
<p>w. Select a sample of significant outstanding overpayments to:</p>	
<p>(1) Obtain information on the overpayment; e.g., a copy of the invoice, copies of payment records showing invoice amount and date, payment amount and date,</p>	
<p>(2) Document the reason for the overpayment, and</p>	
<p>(3) Obtain the contractor’s rationale for not returning the overpayment; and the contractor’s documented significant actions taken to resolve differences.</p>	
<p>(4) Immediately notify applicable paying office via memorandum if a significant overpayment (\$50 thousand on a single issue or \$50 thousand on an individual contract) is disclosed during the audit and (1) the contractor has not notified the Government, or (2) the overpayment is over 30 days and has not been returned. Use the pro forma notification to payment office memo located</p>	

Master Document – Audit Program

in APPS to make this notification.	
x. Selectively evaluate delivery invoices and determine that the amounts billed are reduced for previously received progress payment amounts.	
y. Selectively evaluate interim and final closing vouchers submitted by the contractor and determine if the amounts billed are reconcilable to the cumulative allowable cost records used to prepare interim and final vouchers. Test for the following:	
(1) Cumulative amounts billed on interim vouchers do not exceed the total estimated ceiling costs on the contract and/or the current contract maximum funding levels.	
(2) Amounts claimed on the final voucher reconcile to the annual incurred cost audit or the cumulative allowable cost worksheet (CACWS);	
(3) Assist audits have been received on all significant subcontract costs prior to the closing of applicable contracts;	
(4) Subcontract assist audit cost results reconcile with claimed costs on the final voucher;	
(5) Refunds, rebates, credits, or similar amounts have been received, if any, and accounted for in the final voucher.	
z. Validate that final vouchers are monitored and timely prepared and submitted. Coordinate with Contracting Administrative Offices for a schedule of completed contracts awaiting closure.	

A-1	Concluding Steps	W/P Reference
	Version 7.0, dated June 2004	
	1. Assessment of Control Risk	
	a. Considering all five components of internal control (control environment, contractor risk assessment, information and communications, monitoring, and control activities that relate to control objectives), assess control risk for each of the relevant control objectives (management reviews, policies and procedures, and implementation of policies and procedures). For each of the objectives, summarize the characteristics which support the assessed level of control risk and specifically identify any internal control weaknesses or system deficiencies.	
	b. Determine if the billing system is adequate to reasonably assure proper pricing, administration, and settlement of Government	

Master Document – Audit Program

contracts in accordance with applicable laws and regulations.	
c. Based on the assessments above, determine the impact on the scope of other audits.	
d. Update the ICAPS (see CAM 3-305).	
e. Coordinate the results of audit with the supervisor. The supervisor and the FAO manager should review and initial the ICAPS before the exit conference is performed. If it is determined that additional audit steps are needed, any additional planned audit effort should be accomplished as part of this examination or immediately thereafter. Any delays in completion of this audit effort should be documented and approved by management.	
2. Direct Bill Authorization	
Document the FAO’s decision to:	
a. Allow the contractor to participate or to continue to participate in the direct billing program; or	
b. Follow audit guidance for rescinding the contractor’s authority to direct bill; or	
c. Document the rationale for denying the contractor’s participation in the direct billing program.	
3. Summary Steps	
a. Prepare a draft audit report in accordance with CAM 10-400.	
b. If any potentially reportable conditions relate to specific contract overpayment issues, discuss the results of audit with the regional DFAS Task Force member prior to the exit conference.	
c. Conduct an exit conference with the contractor in accordance with CAM 4-304.	
d. Finalize the audit report incorporating the contractor's response and audit rejoinder.	
e. Coordinate with supervisor to verify DMIS accuracy. In the contractor tables in DMIS verify the accuracy of entries for:	
(1) Direct billing initiative	
(2) CAGE code(s)	
f. Copies of the final report should be provided to the regional Task Force member if reported conditions relate to overpayment issues.	
g. Ensure that the paying office and contracting officer have been notified of any unresolved overpayments, contract administration adjustments, demand letters, and subcontract billings that are over 30 days old; and of any improper offsets. The pro forma	

Master Document – Audit Program

<p>notification to the payment office should be addressed to the paying office and if the paying office is DFAS, sent to the DCAA DFAS Financial Liaison Advisor to be hand delivered/emailed to DFAS. A copy should also be provided to the ACO and the regional Task Force member or representative.</p>	
<p>h. If the contractor has EVMS covered contracts, provide comments in the audit report on whether any findings are likely to impact the contractor's EVMS (10-1204.5b). Discuss findings and recommendations relating to the EVMS with the Contract Administration Office EVMS Monitor prior to issuance of the report. Immediately evaluate the impact of these findings on specific EVMS covered contracts and provide the details in flash EVMS surveillance reports (11-209.2.e).</p>	
<p>i. Update the permanent file in accordance with CAM 4-405.1.b (MAAR 3).</p>	
<p>j. Contact customers who require excessive documentation with vouchers explaining:</p>	
<ul style="list-style-type: none"> • How contract provisions require contractor to submit excessive documentation. 	
<ul style="list-style-type: none"> • How DCAA’s ongoing presence and system examinations at the contractor can satisfy any customer billing requirements. 	
<ul style="list-style-type: none"> • That DCAA would like an opportunity to explain our process and discuss whether it satisfies their needs. 	
<p>4. Closing Actions</p>	
<p>Closing actions should be performed in accordance with FAO procedures. These procedures may require either auditors or administrative personnel to perform various closing steps. Completion of these closing actions should be documented (e.g., by initials and date on the CD or working paper folder, etc.) and should include:</p>	
<p>a. The title, author, and keywords fields of the file properties in the audit report must be completed (for the audit report only) prior to final filing.</p>	
<p>b. Review the APPS exe file for size. APPS-generated executable files that are over 10 megabytes in size should be reviewed to ensure that the format and content justify the size. Supervisors are responsible for reviewing or designating someone to review these files for content and format.</p>	
<p>c. Review the APPS exe file for temporary files. These files can be recognized by the “~\$” or “~WRL” at the beginning of the file name. Once the APPS exe file is complete and there is NO</p>	

Master Document – Audit Program

<p>ACTIVITY to be complete on any of the files contained within the exe file, any temporary files should be deleted so there are no unintentional versions of working papers and/or reports. NOTE: This should be done prior to invoking the Export/Archive Option in APPS.</p>	
<p>d. Once an audit report is signed, the electronic document should immediately be modified to indicate who signed it, and it should be password protected. The electronic file should then be renamed according to the convention “01 DCAA Report [RORG-ASSIGNMENT NO.] – Final.doc” and changed to a read-only file. Only this file should be stored, transmitted, or otherwise used for official purposes. For Memorandums the word “Report” would be replaced by “MFF” or “MFR” in the naming convention as appropriate.</p>	
<p>e. When the audit report is transmitted electronically to the requestor, the transmission email should be saved as a txt file (this will ensure the attachments are not saved again). Saving delivery or read receipts is optional. If saved, the naming convention should distinguish them from transmittal emails.</p>	
<p>f. Once the report is signed, the signature page of the audit report must be scanned in accordance with Agency standard scanning instructions. For audit packages, the scanned signature page file should be named the same as the audit report (see above) with “-sig” added (i.e., 01 DCAA Report 01101-2002X10100389-Final-sig.pdf). There is no requirement to make the file a part of the APPS generated executable file and it must be included separately in the iRIMS folder. There is no need to scan the signature page of a Memorandum unless it is distributed outside of DCAA.</p>	
<p>g. Ensure an electronic copy of the final draft audit report containing the supervisory auditor’s initials and date, cross-referenced to the working papers, is included in the working paper package. The final draft report should include all substantive changes made to the original draft, with cross-referencing updated as necessary. It should differ from the final report only due to minor administrative changes (spelling, format, etc.) made during final processing.</p>	
<p>h. Ensure all working paper files are "read only" and, if necessary, compressed for final storage. Generally, current Agency software should be used to automatically modify all electronic files for storage.</p>	
<p>i. Two complete sets of electronic working papers should be filed. One set (official) will be filed in iRIMS. A second set (backup) will be stored on removable media in the hard copy working paper folder. The new APPS naming convention (ex: 01701_2003A1010001_Archive_093003.exe) will be used</p>	

Master Document – Audit Program

<p>for both. If there will be a short-term need to access the working papers, a third, or "working" set should be stored so as to be available for reference, generally on the LAN. This set should be deleted when no longer needed.</p>	
<p>j. Verify using a separate machine, that electronic files stored on removable media are not corrupted and can be unarchived. Indicate the test was successful by placing tester initials and date prominently on the CD label.</p>	
<p>k. Securely enclose the "backup" set of electronic files (CD) and any "official" set of hard copy in the hard copy folder.</p>	
<p>l. File the "official" set of electronic files in iRIMS (see iRIMS User Guide).</p>	
<p>m. <u>Do Not File Sensitive Audits in iRIMS</u>: Sensitive audits include but are not limited to classified work, suspected irregular conduct, hotline or DCAA Form 2000 related files. These audits should not be filed in iRIMS at this time. See CAM 4-407f for filing instructions.</p>	