VOLUME 10, CHAPTER 1: “FINANCIAL CONTROL OF VENDOR AND CONTRACT PAYMENTS”

SUMMARY OF MAJOR CHANGES

All changes are denoted by blue font.

Substantive revisions are denoted by an * symbol preceding the section, paragraph, table, or figure that includes the revision.

Unless otherwise noted, chapters referenced are contained in this volume.

Hyperlinks are denoted by **bold, italic, blue and underlined font**.

The previous version dated January 2010 is archived.

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<td>All</td>
<td>Administrative changes were made that included minor editing, and the updating of a few hyperlinks.</td>
<td>Update</td>
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<td>0102</td>
<td>Reorganized Internal Control responsibilities which included adding Internal Control objectives found in the Federal Managers Financial Integrity Act.</td>
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CHAPTER 1

FINANCIAL CONTROL OF VENDOR AND CONTRACT PAYMENTS

0101  GENERAL

010101. Purpose

Department of Defense (DoD) officials are responsible for ensuring DoD organizations maintain control of payments made to vendors and contractors. This volume prescribes the policy necessary to ensure the obligation of DoD to pay for goods, services, and transportation and to make payments based on terms and conditions contained in accepted purchase orders, contracts, and unilateral and bilateral modifications. It prescribes the policy for issuing payments based on the entitlement, preparing payment vouchers, and keeping contract, disbursement and accounting records complete, consistent, and accurate.

010102. Scope

Related policy and standards for recording obligations, resolving unmatched disbursements and negative unliquidated obligations, and posting budgetary accounting entries, respectively, are in Volume 3, Chapters 8, 11, and 15. Policy regarding accounting for payables is in Volume 4, Chapter 9. Policy regarding disbursement vouchers, accountable officials and certifying officers, respectively, are in Volume 5, Chapters 11 and 33. Antideficiency Act violations are addressed in Volume 14, Chapter 2.

*0102  INTERNAL CONTROLS

The importance of internal controls is addressed in many statutes and executive documents, which include the Federal Managers Financial Integrity Act (FMFIA), Office of Management and Budget (OMB) Circular A-123, DoD FMR Volume 1, Chapter 3, and DoD Instruction 5010.40.

010201. Statutory Compliance

The FMFIA establishes overall requirements with regard to internal controls where the DoD Component Head is charged with establishing controls to reasonably ensure that:

A. Obligations and costs are in compliance with applicable laws;

B. Funds, property, and other assets are safeguarded against waste, loss, unauthorized use or misappropriation; and

C. Revenues and expenditures, applicable to DoD operations, are properly recorded and permit the preparation of reliable financial and statistical reports to maintain accountability over assets.
010202. Regulatory Compliance

It is the policy of DoD to make payments and collections in accordance with applicable laws and regulations that are timely and accurate. These include requirements for identification, reporting, and reduction of improper payments (see Volume 4, Chapter 14 and Volume 5, Chapter 6 paragraph 0603). In addition, financial managers with responsibilities for ensuring internal controls are established and functioning properly to comply with this policy shall:

A. Create, document, and maintain an organizational structure and business processes that appropriately segregate assigned duties, emphasize adherence to policies and procedures, and employ sound internal accounting and system access controls;

B. Implement finance and accounting systems that comply with the federal financial management systems requirements, maintain accurate and complete accounting and entitlement records from contract execution through closeout, and monitor the causes of late payments and interest penalties incurred. The complete listing of functional requirements for payment management systems is in the Defense Finance and Accounting Service (DFAS) document titled, DFAS 7900.4-M “Financial Management Systems Requirements Manual”. Efforts to develop or modify a critical financial management system (see Volume 1, Chapter 3) shall be subject to the financial and feeder systems compliance process;

C. Establish systematic controls that provide adequate audit trails to allow the tracing of financial events from source documents to general ledger account balances through successive levels of summarization and financial reports/statements. Ensure all transactional data is processed using accurate coding, and errors are researched and corrected; and

D. Employ systems that ensure the authenticity of electronically transmitted data, including the electronic signature. Such controls shall provide reasonable assurance that deliberate or inadvertent manipulation, modification, or loss of data during transmission is detected (see Volume 10, Chapter 17).

010203. Periodic Reviews

Managers with responsibilities for determining entitlements, authorizing, or executing payments and collections must:

A. Periodically (minimum annually) validate cash management and payment performance quality and effectiveness, and

B. Periodically (minimum annually) test effectiveness of internal controls, document results of testing, and take necessary corrective actions (see OMB Circular A-123, Management’s Responsibility for Internal Controls).
0103 PREVALIDATION

010301. General

Obligations (and any adjustments) are established and recorded for the amounts of orders placed and contracts awarded that will require payment in the current or some future accounting period, as prescribed in Volume 3, Chapters 8 and 15, of this Regulation. Liabilities for payment, including accounts payable, are established as prescribed in Volume 4, Chapters 8 and 9. Prevalidation is the process of matching the planned disbursement with a recorded obligation before the financing or invoice payment is made. The requirement is to determine that prior to payment the undisbursed balance of each applicable obligation is sufficient to cover the amount of the planned disbursement, as well as all previously scheduled disbursements (see Volume 3, Chapter 11). The process is intended to minimize the occurrence of problem disbursements and Antideficiency Act violations (see Volume 14, Chapter 2).

010302. Policy Guidance

The DoD has established prevalidation policy as follows:

A. All Non-Mechanization of Contract Administration Services (non-MOCAS) payments shall be prevalidated.

B. The DoD has established the following prevalidation thresholds for MOCAS payments:

1. All payments made on contracts awarded after Fiscal Year (FY) 2004 are prevalidated.

2. On contracts issued during FY 2004 and prior, payments for more than $5,000 are prevalidated.

0104 PAYMENT LIMITATIONS

The following contract clauses, when applicable, may impose limitations on entitlement to financing or invoice payments.

010401. Limitation on Undefinitized Contracting Actions

In accordance with Federal Acquisition Regulation (FAR) Subpart 16.603-4, letter contracts shall include FAR clause 52.216-24. Under the terms stated there, the maximum amount of the government’s obligation is the amount specified in the clause. However, if a contractor submits a qualifying proposal before 50 percent of the not-to-exceed price has been obligated by the Government, then the limitation on obligations before definitization may be increased to no more than 75 percent (see Defense Federal Acquisition Regulation Supplement (DFARS) Subpart 217.7404-4 and related DFARS clause 252.217-7027). According to the DFARS Subpart 217.7401, “definitization” means the agreement on, or determination of,
contract terms, specifications, and price, which converts the undefinitized contract action to a definitive contract. An “undefinitized contract action” means any contract action for which the contract terms, specifications, or price are not agreed upon before performance is begun under the action. Examples are letter contracts, orders under basic ordering agreements, and provisioned item orders, for which the price has not been agreed upon before performance has begun.

010402. Limitation of Cost or Funds

The basic requirements for contract funding are described in FAR Subpart 32.7. No officer or employee of the government may create or authorize an obligation in excess of the funds available or in advance of appropriations (see Volume 14, Chapter 2). The contracting officer expressly shall condition contracts on the availability of funds. Fully funded cost-type contracts may include FAR clause 52.232-20, or incrementally funded cost-type contracts may include FAR clause 52.232-22. Under the terms stated there, the government’s obligation to the contractor (and the contractor’s obligation to perform) is generally limited to the funds allotted to the contract.

010403. Limitation on Withholding of Payments

In accordance with FAR Subpart 32.111(b)(2), noncommercial supply, research and development, service, time and materials or labor hour contracts that include two or more terms that authorized temporary withholding of amounts otherwise payable shall include FAR clause 52.232-9. Under the terms stated there, the total amount that may be withheld at any one time shall not exceed the amount that may be withheld under any one clause or contract schedule term. This limitation does not apply to withholding under any clause related to employee wages, the recovery of overpayments, withholdings not provided for in the contract, or to any withholding for which the contracting officer determines the limitation would not be appropriate.

010404. Limitation of Government’s Obligation

In accordance with DFARS Subpart 232.705-70, incrementally funded fixed-price contracts (one or more incrementally funded contract line items) shall include DFARS clause 252.232-7007. Under the terms stated there, the government’s obligation to the contractor for the incrementally funded Contract Line Item Number(s) (CLIN(s)) (and the contractor’s obligation to perform) generally is limited to the funds allotted. The contract clause requires the contractor to notify the contracting officer 90 days prior to the date when the work will reach 85 percent of the amount then allotted.