

Audit



Report

OFFICE OF THE INSPECTOR GENERAL

**FINANCIAL REPORTING BY SELECTED DEFENSE
AGENCIES OF GOVERNMENT PROPERTY IN THE
CUSTODY OF CONTRACTORS**

Report No. 98-042

December 16, 1997

19990928 020

Department of Defense

DTIC QUALITY INSPECTED 4

AQI 99-12-2442

Additional Copies

To obtain additional copies of this audit report, contact the Secondary Reports Distribution Unit of the Analysis, Planning, and Technical Support Directorate at (703) 604-8937 (DSN 664-8937) or FAX (703) 604-8932.

Suggestions for Future Audits

To suggest ideas for or to request future audits, contact the Planning and Coordination Branch of the Analysis, Planning, and Technical Support Directorate at (703) 604-8908 (DSN 664-8908) or FAX (703) 604-8932. Ideas and requests can also be mailed to:

Inspector General, Department of Defense
OAIG-AUD (ATTN: APTS Audit Suggestions)
400 Army Navy Drive (Room 801)
Arlington, Virginia 22202-2884

Defense Hotline

To report fraud, waste, or abuse, contact the Defense Hotline by calling (800) 424-9098; by sending an electronic message to Hotline@DODIG.OSD.MIL; or by writing the Defense Hotline, The Pentagon, Washington, D.C. 20301-1900. The identity of each writer and caller is fully protected.

Acronyms

AFIS	American Forces Information Service
CPMS	Contract Property Management System
DIA	Defense Intelligence Agency
DISA	Defense Information Systems Agency
DNA	Defense Nuclear Agency
DSWA	Defense Special Weapons Agency
OSIA	On-Site Inspection Agency



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2884



December 16, 1997

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION
AND TECHNOLOGY
UNDER SECRETARY OF DEFENSE (COMPTROLLER)
DIRECTOR, DEFENSE INFORMATION SYSTEMS
AGENCY
DIRECTOR, DEFENSE SPECIAL WEAPONS AGENCY
DIRECTOR, AMERICAN FORCES INFORMATION
SERVICE

SUBJECT: Audit Report on Financial Reporting by Selected Defense Agencies of
Government Property in the Custody of Contractors (Report No. 98-042)

We are providing this audit report for your information and use. This is the second in a series of reports resulting from a joint audit with the Army, Navy, and Air Force audit organizations. We considered management comments on a draft of this report in preparing the final report.

The Defense Information Systems Agency, Defense Special Weapons Agency, and American Forces Information Service comments conformed to the requirements of DoD Directive 7650.3 and left no unresolved issues. Therefore, additional comments are not required.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Richard B. Bird, Audit Program Director, at (703) 604-9175 (DSN 664-9175) or e-mailed to rbird@DODIG.OSD.MIL. Questions may also be directed to Ms. Linda A. Pierce, Audit Project Manager, at (216) 522-6091, extension 234 (DSN 580-6091, extension 234) or e-mailed to lap@DODIG.OSD.MIL. See Appendix C for the report distribution. The audit team members are listed inside the back cover.

Robert J. Lieberman
Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. 98-042
(Project No. 6FI-2009.01)

December 16, 1997

Financial Reporting by Selected Defense Agencies of Government Property in the Custody of Contractors

Executive Summary

Introduction. This report is the second in a series of reports on Government property issues resulting from a DoD-wide audit performed to meet the requirements of the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994. Report No. 97-202, "Financial Reporting of Government Property in the Custody of Contractors," August 4, 1997, discusses the use of the Contract Property Management System for the financial reporting of Government property in the custody of contractors. That report states the system could not be relied upon by the financial management community for accurate financial reporting. A future report will consolidate the results of work done by all Military Department audit agencies participating in the audit.

Although the Contract Property Management System does not meet financial statement reporting requirements, about \$171 million in Government property in the custody of contractors was reported there by the Military Departments and the Defense Contract Management Command for the Defense Information Systems Agency, Defense Special Weapons Agency, and American Forces Information Service. About 90 contracts administered by the Defense agencies, which may contain Government property in the custody of contractors, were not included in the Contract Property Management System.

The Inspector General, DoD, has issued several reports regarding the inadequacy of financial reporting for Government property in the custody of contractors, as summarized in Appendix B. None of the organizations audited properly reported the financial information related to Government property in the custody of contractors. Such recurring deficiencies show that DoD has not gained adequate financial control and accountability over the \$92 billion of Government property in the custody of contractors. After several years of planning, DoD has not developed a standard accounting system for recording, tracking, and reporting Government property in the custody of contractors. Until adequate DoD systems are working, DoD must develop a method of reporting the value of Government property in the custody of contractors in its financial statements.

Audit Objectives. The overall audit objective was to determine whether account balances for Government property in the custody of contractors were accurate and complete in the financial statements of the Military Departments and Defense agencies. We also assessed management controls affecting the financial reporting of Government property, and we assessed compliance with applicable laws and regulations.

Our first report discusses the use of the Contract Property Management System for reporting Government property in the custody of contractors in the financial statements. The report recommended that the Under Secretary of Defense (Comptroller) establish a working group to address the issues associated with financial reporting. This report discusses the reporting of Government property in the custody of contractors on the financial statements of the Defense Information Systems Agency, Defense Special Weapons Agency, and American Forces Information Service.

Audit Results. The three Defense agencies audited did not report the amount of Government property in the custody of contractors in accordance with financial reporting requirements. As a result, the FY 1996 financial statements were inaccurate. Improved controls over the financial reporting of Government property in the custody of contractors would ensure the property was accounted for and reported in the financial statements. For details of the audit results, see Part I. We reviewed the management controls over the reporting of Government property in the custody of contractors in the financial statements. Our first report identifies a DoD-wide material management control weakness for financial reporting of Government property in the custody of contractors. In this report, we identified a material management control weakness for the Defense agencies reviewed. For a discussion of management controls over the financial reporting of Government property in the custody of contractors, see Appendix A.

Summary of Recommendation. We recommend that the Directors of the Defense Information Systems Agency, Defense Special Weapons Agency, and American Forces Information Service provide a point of contact to the Under Secretary of Defense (Comptroller) for the financial reporting issues working group and identify the systems that include Government property in the custody of contractors.

Management Comments. The Defense Information Systems Agency, Defense Special Weapons Agency and the American Forces Information Service concurred with the recommendation to provide a point of contact to the Under Secretary of Defense (Comptroller) for the financial reporting working group. The Defense Information Systems Agency and Defense Special Weapons Agency concurred with the recommendation to identify the systems that include Government property in the custody of contractors. The American Forces Information Service partially concurred with the recommendation to identify the systems that include Government property in the custody of contractors. The American Forces Information Service is working to determine how Government property in the custody of contractors will be captured and reported in future financial statements. See Part I for a summary of management comments on the recommendations. See Part III for the complete text of management comments.

Audit Response. Although the American Forces Information Service only partially concurred with the recommendation to identify the systems that include Government property in the custody of contractors, the comments are responsive because proposed actions satisfy the intent of the recommendation. Therefore, no further comments are required.

Table of Contents

Executive Summary	i
Part I - Audit Results	
Audit Background	2
Audit Objectives	3
Financial Reporting of Government Property	4
Part II - Additional Information	
Appendix A. Audit Process	
Scope and Methodology	10
Management Control Program	10
Appendix B. Summary of Prior Coverage	12
Appendix C. Report Distribution	15
Part III - Management Comments	
Defense Information Systems Agency Comments	18
Defense Special Weapons Agency Comments	20
American Forces Information Service Comments	21

Part I - Audit Results

Audit Background

The Chief Financial Officers Act of 1990 (Public Law 101-576), as amended by the Government Management Reform Act of 1994 (Public Law 103-356), requires DoD to submit annual, audited financial statements to the Director, Office of Management and Budget. The DoD consolidated financial statement includes a reporting entity entitled "Other Defense Organizations," which covers the agencies discussed in this report: the Defense Information Systems Agency (DISA), Defense Special Weapons Agency (DSWA), and American Forces Information Service (AFIS). In this report, we use the term "Defense agencies" to mean DISA, DSWA, and AFIS.

The DISA is the Defense agency responsible for information technology and is the central manager of major portions of the Defense Information Infrastructure. The Director, DISA, reports to the Assistant Secretary of Defense for Command, Control, Communications, and Intelligence. In 1996, the Defense Nuclear Agency (DNA) was renamed DSWA. The DSWA is the DoD center for nuclear and advanced weapons effects expertise. The Director, DSWA, reports to the Assistant Secretary of Defense for Nuclear and Chemical and Biological Defense Programs. The AFIS serves as the DoD internal information arm, keeping DoD military and civilian personnel and their families informed on matters affecting their lives. The Assistant Secretary of Defense (Public Affairs) has oversight responsibility for AFIS.

Federal Acquisition Regulation Requirements for Government Property. The Federal Acquisition Regulation, Part 45, "Government Property," provides guidance for providing Government property to contractors. The Regulation defines Government property in the custody of contractors as property owned or acquired by the Government under the terms of a contract. Contractors are ordinarily required to furnish all property necessary to perform Government contracts. However, the Government may provide property to the contractor or allow the contractor to purchase property to complete contract work when in the best interest of the Government. In this report, we use the term "Government property" to mean all Government-owned property in the custody of contractors, whether furnished to contractors by the Government or acquired by contractors for the Government. The Regulation also holds contractors accountable for Government property in their custody and requires contractors to maintain the official Government property records. The Government is prohibited from maintaining duplicate property records. Defense contractors annually report the amount of Government property on the Defense Department Form 1662, "DoD Property in the Custody of Contractors." DoD personnel review and enter the Government property data from the Defense Department

Form 1662 into the Contract Property Management System (CPMS). The CPMS is a DoD system that provides an annual snapshot of Government property balances as of September 30.

Financial Reporting Requirements for Government Property. Federal Financial Accounting Standard Number 6, "Accounting for Property, Plant, and Equipment," November 1995, requires general property, plant, and equipment to be recorded at acquisition cost, capitalized in accordance with capitalization criteria, and depreciated. The standard includes Government property in the custody of contractors as part of property, plant, and equipment.

Audit Objectives

The overall audit objective was to determine whether the Government property account balances in the financial statements for the Military Departments and Defense agencies are accurate and complete. We also assessed management controls affecting the financial reporting of Government property, and we assessed compliance with applicable laws and regulations.

This is the second in a series of reports on Government property issues. This report addresses the financial reporting of Government property by Defense agencies. Our previous report, "Financial Reporting of Government Property in the Custody of Contractors," August 4, 1997, discusses the use of CPMS as a source for financial reporting. We plan to issue a consolidated report on the results of our work and that of the Military Department audit agencies participating in the DoD-wide Government property audit.

Appendix A discusses the audit scope, methodology, and management control program. Appendix B summarizes prior coverage related to the audit objectives.

Financial Reporting of Government Property

The DISA, DSWA, and AFIS did not report Government property in the FY 1996 financial statements in accordance with financial reporting requirements. This occurred because DoD had not developed clear guidance on how Government property should be captured and reported or established a standard system to ensure timely and reliable financial reporting. As a result, the FY 1996 property balances in these Defense agency financial statements were misstated by at least \$171 million.

Defense Agency Financial Reporting

The Defense agencies we reviewed did not report Government property in the FY 1996 financial statements in accordance with financial reporting requirements. According to agency officials, each agency provided property to contractors in performance of contracts. Although Government property was provided to contractors, the Defense agencies did not have procedures or systems to capture and report Government property in the financial statements. The Military Departments and the Defense Contract Management Command reported about \$171 million in Government property for the three Defense agencies in the FY 1996 CPMS. However, the Defense agencies did not report the Government property in CPMS on the financial statements. As a result, the total value of Government property was omitted from the FY 1996 financial statements.

The Inspector General, DoD, has issued several reports related to the financial reporting of Government property. Report No. 97-129, "Financial Accounting at the On-Site Inspection Agency," April 15, 1997, states that the On-Site Inspection Agency (OSIA) had not established procedures to report Government property in its financial statements. The report recommended OSIA establish procedures to record balances of Government property in the general ledger. Report No. 97-045, "Financial Accounting at the Defense Intelligence Agency," December 12, 1996, also states that the Defense Intelligence Agency (DIA) had not established procedures to report Government property in its financial statements. The report recommended that DIA establish procedures to record balances of Government property in the accounting records. Report No. 96-039, "Financial Accounting for the Defense Nuclear Agency," December 11, 1995, states that DNA had not established procedures to record information from contractors' annual reports into the financial reports. Also,

controls over Government property were inadequate to ensure accurate and supportable financial statements. The report did not contain any recommendations regarding Government property.

Government Property Reporting in Financial Statements

Guidance for reporting Government property in the financial statements is unclear. Financial reporting guidance places additional requirements on reporting Government property. Current methods of reporting Government property, in accordance with acquisition guidance, do not provide adequate data for financial reporting. In addition, the Government is prohibited from maintaining duplicate property records. As a result, data required for financial reporting of Government property are unavailable. The acquisition, logistics, and finance communities must coordinate reporting requirements and establish clear guidance to ensure that timely and reliable financial information is reported.

Financial Reporting Systems for Government Property

DoD systems must provide timely and reliable financial information. However, a standard system has not been implemented to capture and report Government property in the financial statements. The CPMS does not meet financial statement reporting requirements and cannot be relied upon as an accurate source of reporting Government property in the financial statements.

System Requirements for Government Property. DoD 7000.14-R, "Financial Management Regulation," volume 1, "General Financial Management Information, Systems, and Requirements," May 1993, prescribes policy for system compliance. Accounting systems must have general ledger control and provide full financial disclosure, accountability, adequate financial information, and reports for management purposes. In addition, systems must account in quantitative and monetary terms for the procurement, receipt, issue, and control of plant, property, equipment, inventory, and material. Volume 6, "Reporting Policies and Procedures," February 1996, states that the financial reports shall be generated from an accounting system that is an integral part of a total financial management system providing interfaces with logistics and acquisition systems. Volume 4, "Accounting Policy and Procedures," January 1995, further requires DoD accounting systems to contain Government property data by contractor and provide timely and reliable financial information.

Financial Reporting of Government Property

CPMS Reporting of Government Property. For FY 1996, the data contained in CPMS did not include about 90 contracts administered by the Defense agencies that may contain Government property. Defense agency contracts administered by the Military Departments and by the Defense Contract Management Command that contained Defense agency Government property are included in CPMS. The FY 1996 CPMS showed about \$171 million in Government property for DISA, DSWA, and AFIS. However, the three Defense agencies did not use CPMS to capture and report Government property in the financial statements. Officials at DISA and AFIS were not familiar with the system and its capabilities. Officials at DSWA stated that they were aware of the system; however, DSWA did not have procedures in place to incorporate the data into the financial statements.

The only system that reports Government property, the CPMS, is not adequate for financial reporting purposes. Inspector General, DoD, Report No. 97-202, "Financial Reporting of Government Property in the Custody of Contractors," August 4, 1997, states that the system does not meet financial statement reporting requirements because the system was not designed to support financial statements. For example, CPMS duplicated assets reported in the general ledger, did not apply capitalization thresholds, and could not distinguish assets between the General and Working Capital funds. In addition, controls were not established to ensure that all Government property was recorded in CPMS. As a result, the financial management community cannot rely on CPMS as an accurate source for reporting Government property in the financial statements.

Conclusion

The results of our review at the three Defense agencies, combined with the results of prior Inspector General, DoD, audits, indicate that most Defense agencies likely have omitted Government property from their financial statements. Controls were not established at any of the Defense agencies audited to ensure Government property was reported in the financial statements. As a result of this lack of controls, a material management control weakness was identified at DISA, DSWA, and AFIS. Until clear guidance is established and a standard system is implemented that meets financial reporting requirements, DoD will not have accurate, complete, and auditable Government property balances in its financial statements. Consequently, our first report recommended that the Under Secretary of Defense (Comptroller) establish a working group to address these overall financial reporting issues. We reiterate the need for the DoD accounting community to emulate the aggressive action being taken by the DoD acquisition communities to reengineer the business practices related to Government property in contractors' possession.

Management Actions

DISA, DSWA, and AFIS recognize the problem of reporting Government property. In addition, DISA has established its own Property Management Working Group. One objective of the working group will be to determine how Government property will be captured and reported in future financial statements.

Recommendation, Management Comments, and Audit Response

We recommend that the Directors of the Defense Information Systems Agency, Defense Special Weapons Agency, and American Forces Information Service:

1. Provide a point of contact to the Under Secretary of Defense (Comptroller) for the financial reporting issues working group recommended in our previous report.
2. Identify the systems that include Government property in the custody of contractors, determine whether that information is included in data reported for the financial statements, and report the information to their agency Comptrollers and the DoD Chief Financial Officer.

Defense Information Systems Agency Comments. DISA concurred with Recommendation 1, stating the DISA Comptroller point of contact will be provided to the Office of the Under Secretary of Defense (Comptroller). DISA also concurred with Recommendation 2, stating the information will be provided to the DISA Comptroller and the DoD Chief Financial Officer.

Defense Special Weapons Agency Comments. DSWA concurred with Recommendation 1, stating the DSWA point of contact was provided to the Office of the Under Secretary of Defense (Comptroller) on October 21, 1997. DSWA also concurred with Recommendation 2, stating that officials at DSWA will work with the Office of the Secretary of Defense (Comptroller) to resolve this systemic problem.

American Forces Information Service Comments. AFIS concurred with Recommendation 1, stating points of contact were provided to the Office of the Under Secretary of Defense (Comptroller) on October 22, 1997. AFIS partially concurred with Recommendation 2, stating the Defense Property Accountability

Financial Reporting of Government Property

System is used to account for Government property in the custody of contractors. AFIS officials provided quarterly reports of property values to the Defense Finance and Accounting Service and believed that the information was being reported in the financial statements. However, AFIS recently discovered that the information provided to the Defense Finance and Accounting Service was not being used for financial statement reporting. AFIS is in the process of determining how the property information will be captured and reported in future financial statements and has provided the information to the responsible agency official and will report it to the DoD Chief Financial Officer.

Audit Response. Although AFIS only partially concurred with Recommendation 2, the comments are responsive because proposed actions satisfy the intent of the recommendation. Therefore, no further comments are required.

Part II - Additional Information

Appendix A. Audit Process

Scope and Methodology

We limited our review to the financial reporting of Government property at DISA, DSWA, and AFIS. We determined our audit scope by coordinating our Defense agency audit coverage with prior Inspector General, DoD, audits. To accomplish the audit objectives, we reviewed the data contained in CPMS for FY 1995 and FY 1996. We also analyzed the Defense agency FY 1996 financial reports and interviewed both logistics and finance personnel at the Defense agencies. We used computer-processed data from CPMS to obtain the Government property being reported by the Military Departments and Defense Contract Management Command for the three Defense agencies. Our report, "Financial Reporting of Government Property in the Custody of Contractors," August 4, 1997, states that CPMS cannot be relied upon for reporting Government property in the financial statements.

Audit Type, Dates, and Standards. We performed this financial-related audit from November 1996 through July 1997 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. Accordingly, we included tests of management controls considered necessary.

Contacts During the Audit. We visited or contacted individuals and organizations within the DoD. Further details are available on request.

Management Control Program

DoD Directive 5010.38, "Management Control Program," August 26, 1996, requires 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 the controls.

Scope of Review of the Management Control Program. We reviewed the annual Statements of Assurance for the three Defense agencies. Specifically, we reviewed the controls over capturing and reporting Government property in the financial statements.

Adequacy of Management Controls. Report No. 97-202, "Financial Reporting of Government Property in the Custody of Contractors," August 4, 1997, identifies a DoD-wide material management control weakness for the financial reporting of Government property. This report identified material management control weaknesses as defined by DoD Directive 5010.38 for the Defense agencies reviewed. Controls were not in place to ensure Government property in the custody of contractors was accounted for and reported in the financial statements. The recommendation, if implemented, will assist in improving the financial reporting of Government property by the three Defense agencies. A copy of the report will be provided to the senior officials responsible for management controls at DISA, DSWA, and AFIS.

Adequacy of Management's Self-Evaluation. General Ledger Control Over Property was reported as a material weakness in the DSWA FY 1994 Annual Statement of Assurance. This problem includes equipment inventories in the hands of contractors. The DSWA was awaiting guidance from DoD before implementing corrective action. Officials at DISA and AFIS did not identify financial reporting of Government property as an assessable unit and, therefore, did not identify or report the material management control weakness identified by the audit.

Appendix B. Summary of Prior Coverage

The complete and accurate reporting of Government property has been a long-standing problem throughout DoD. The Inspector General, DoD, has issued several reports that have included Government property issues.

Report No. 97-202, "Financial Reporting of Government Property in the Custody of Contractors," August 4, 1997, addresses the use of CPMS for the financial reporting of Government property. The report states CPMS does not meet DoD requirements for financial statement reporting. Therefore, the system cannot be relied on for reporting the value of Government property balances in the financial statements. In addition, CPMS does not completely or accurately report Government property. As a result, errors totalling \$962 million were found in CPMS, and DoD had no assurance that the remainder of the data were complete or accurate. The report recommended that the Commander, Defense Contract Management Command, complete the redesign of CPMS and require property administrators to use the Defense Contract Management Command Property Administration Data System to identify contracts with Government property. The report also recommended that the Under Secretary of Defense (Comptroller) establish a working group to develop solutions regarding the financial accountability and reporting problems of Government property and develop policy for financial reporting. The Defense Contract Management Command concurred the recommendation and CPMS is currently in the redesign process. The Under Secretary of Defense (Comptroller) did not comment on the report. A future summary report will readdress the recommendation to the Under Secretary of Defense (Comptroller).

Report No. 97-140, "Financial Management at the American Forces Information Service," May 7, 1997, discusses whether the Defense Finance and Accounting Service and AFIS had implemented effective management controls and complied with laws and regulations for AFIS funds managed and accounted for in FY 1995. The report states that AFIS adjusted trial balances did not comply with DoD accounting standards because the Defense Finance and Accounting Service and AFIS did not maintain audit trails. As a result, the AFIS FY 1995 consolidated trial balance was not fully supported and AFIS financial data could not be depended on to produce reliable financial statements required by the Chief Financial Officers Act. The report recommended that the Defense Finance and Accounting Service, Indianapolis Center, Rome Operating Location, and AFIS maintain records for audit trails in accordance with Key Accounting Requirement 8, "Audit Trails." The Director, AFIS, partially concurred with the recommendation and AFIS has taken corrective actions.

Report No. 97-129, "Financial Accounting at the On-Site Inspection Agency," April 15, 1997, assessed required internal controls and compliance with laws and regulations to produce reliable financial statements required by

the Chief Financial Officers Act. In addition, supporting documentation was reviewed for the FY 1996 account balances OSIA submitted to the Defense Finance and Accounting Service. The report concludes that OSIA accounting records did not contain accurate financial information, and information reported to the Defense Finance and Accounting Service for FY 1996 was incorrect. Specifically, OSIA had not established procedures to report the Government-owned property furnished to contractors in its financial reports. As of September 30, 1996, OSIA contractors reported \$13 million in Government-owned equipment on hand to the Defense Contract Management Command. Because OSIA had not established procedures to report the financial information related to Government-owned equipment furnished to contractors, OSIA did not report that information to the Defense Finance and Accounting Service Indianapolis Center. The report recommended that OSIA establish procedures to record balances of Government-owned equipment in the custody of contractors in the general ledger. The OSIA concurred with the finding and recommendation and stated that corrective actions have been or would be implemented.

Report No. 97-045, "Financial Accounting at the Defense Intelligence Agency," December 12, 1996, assessed the internal controls and compliance with laws and regulations to determine whether DIA accounting systems can produce the reliable information necessary to prepare financial statements required by the Chief Financial Officers Act. The report concludes that DIA accounting records did not contain accurate financial information, and information reported to the Defense Finance and Accounting Service for FY 1995 was incorrect. In addition, the management control program could be improved by correcting material weaknesses in accounting and property controls and reporting. Specifically, DIA had not established procedures to report in its financial statements the Government-furnished property to contractors. As of September 30, 1995, DIA contractors reported \$12 million in Government-owned equipment on hand to the Defense Contract Management Command. Because DIA had not established procedures to report Government-furnished equipment, DIA personnel were not aware of the information contractors reported; consequently, DIA did not report equipment held by contractors. The report recommended DIA establish procedures to record balances of Government-furnished equipment in the accounting records. The DIA concurred with the recommendation and stated that corrective actions have been or would be implemented.

Report No. 96-155, "The Defense Information Systems Agency General Ledger Military Equipment Account," June 10, 1996, discusses the accuracy of the military equipment general ledger account balance and the management control procedures for recording transactions in the general ledger accounts. The audit determined that DISA recorded all military equipment transactions in one specific general ledger account, account 1762, Equipment in Use. This account improperly included the acquisition cost of military equipment loaned

Appendix B. Summary of Prior Coverage

or furnished to other DoD Components, Federal agencies, and DoD contractors. In addition, DISA did not record military equipment loaned or furnished to other DoD Components, Federal agencies, and DoD contractors on its official property records. This resulted in the account 1762 being overstated, while the DISA general ledger account balances for military equipment loaned to other DoD Components and military equipment furnished to other Federal agencies, DoD contractors, and others was understated. The DISA property records were also understated. The report recommended that DISA analyze military equipment transactions and make appropriate accounting entries to accurately record military equipment transactions in the general ledger; record in the official property book military equipment loaned and furnished to other DoD Components, Federal agencies, and contractors; and establish appropriate control techniques to ensure the military equipment transactions are accurately recorded in the general ledger and property records. The DISA concurred with the recommendations and has initiated needed actions.

Report No. 96-039, "Financial Accounting for the Defense Nuclear Agency," December 11, 1995, discusses the financial accounting system used and the related management controls to determine whether the financial accounting system can produce reliable financial information. The report concludes that the financial accounting system used by DNA was in substantial compliance with DoD accounting requirements and capable of providing information required for monthly budgetary reporting. However, DNA had not established necessary subsidiary records and some recorded account balances were incorrect or insupportable. Specifically, DNA had not established procedures to incorporate information from contractors' annual reports into DNA financial reports. Also, controls over Government-owned property held by DNA contractors were not adequate to ensure accurate and supportable financial statements. The report did not contain any recommendations regarding the property held by DNA contractors.

Appendix C. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition and Technology
 Director, Defense Procurement
 Director, Defense Logistics Studies Information Exchange
Under Secretary of Defense (Comptroller)
 Deputy Chief Financial Officer
 Deputy Comptroller (Program/Budget)
Assistant Secretary of Defense (Public Affairs)
Deputy Under Secretary of Defense (Industrial Affairs and Installations)

Department of the Army

Auditor General, Department of the Army

Department of the Navy

Assistant Secretary of the Navy (Financial Management and Comptroller)
Auditor General, Department of the Navy

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and Comptroller)
Auditor General, Department of the Air Force

Other Defense Organizations

Director, Defense Contract Audit Agency
Director, Defense Finance and Accounting Service
Director, Defense Information Systems Agency
Director, Defense Logistics Agency
Director, Defense Special Weapons Agency

Other Defense Organizations (cont'd)

Director, National Security Agency
Inspector General, National Security Agency
Director, On-Site Inspection Agency
Inspector General, Defense Intelligence Agency
Director, American Forces Information Service

Non-Defense Federal Organizations and Individuals

Office of Management and Budget
Technical Information Center, National Security and International Affairs Division,
General Accounting Office

Chairman and ranking minority member of each of the following congressional committees and subcommittees:

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
House Committee on Appropriations
House Subcommittee on National Security, Committee on Appropriations
House Committee on Government Reform and Oversight
House Subcommittee on Government Management, Information, and Technology,
Committee on Government Reform and Oversight
House Subcommittee on National Security, International Affairs, and Criminal
Justice, Committee on Government Reform and Oversight
House Committee on National Security

Part III - Management Comments

Defense Information Systems Agency Comments



DEFENSE INFORMATION SYSTEMS AGENCY
701 S. COURTHOUSE ROAD
ARLINGTON, VIRGINIA 22204-2100



IN REPLY
REFER TO: Inspector General

21 October 1997

MEMORANDUM FOR INSPECTOR GENERAL, DEPARTMENT OF DEFENSE
ATTN: Director, Finance and Accounting

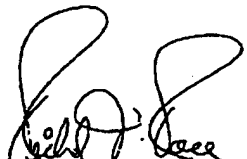
SUBJECT: Draft Audit Report on Financial Reporting by
Selected Defense Agencies of Government Property
in the Custody of Contractors (Project No.
6FI-2009.01)

Reference: DODIG Audit Report, subject as above, 21 Aug 97

The Agency has reviewed the subject draft audit report and concurs with the findings and recommendations. Detailed management comments to the recommendations are enclosed. The point of contact for this action is Ms. Sandra J. Sinkavitch, Audit Liaison, (703) 607-6316.

FOR THE DIRECTOR:

1 Enclosure a/s


RICHARD T. RACE
Inspector General

Quality Information for a Strong Defense

Defense Information Systems Agency Comments

**DODIG DRAFT AUDIT REPORT ON FINANCIAL REPORTING BY
SELECTED DEFENSE AGENCIES OF GOVERNMENT PROPERTY IN THE
CUSTODY OF CONTRACTORS (Project No. 6FI-2009.01)**

Recommend that the Directors of the American Forces Information Service, Defense Information Systems Agency, and the Defense Special Weapons Agency:

Recommendation 1: Provide a point of contact to the Under Secretary of Defense (Comptroller) for the financial reporting issues working group recommended in our previous report.

Response: Concur. The DISA Comptroller point of contact will be provided to the Under Secretary of Defense (Comptroller).

Recommendation 2: Identify the systems that include Government property in the custody of contractors, determine whether that information is included in data reported for the financial statement, and report the information to their agency Comptrollers and the DOD Chief Financial Officer.

Response: Concur. The Defense Property Accounting System (DPAS) is the official property accountability system for DISA and captures DISA/Government property in the hands of DISA activities. DPAS does not capture property in the hands of contractors; however, we are restructuring our approach from a management control aspect so that we can capture contract data as well as other systems which may contain property inventory. Once this is resolved, information will then be provided to the Comptroller and the DOD Chief Financial Officer.

In addition, information in DPAS is not included in the Washington Headquarters Service Allotment Accounting System (WAAS), which is the financial accounting system used for DISA's appropriated funds. Our work around approach will be to have manual adjustments made to the appropriate accounts in our general ledger trial balance. By doing so, the trial balance will reflect what is shown in DPAS prior to the financial statements being prepared from the trial balance.

Enclosure

Defense Special Weapons Agency Comments



Defense Special Weapons Agency
6801 Telegraph Road
Alexandria, Virginia 22310-3398

OCT 23 1997

MEMORANDUM FOR INSPECTOR GENERAL, DEPARTMENT OF DEFENSE
ATTN: DIRECTOR, FINANCE AND ACCOUNTING
DIRECTORATE

SUBJECT: Audit Report on Financial Reporting by Selected Defense Agencies of
Government Property in the Custody of Contractors

Defense Special Weapons Agency management is in concurrence with the findings and recommendations of the subject report. The following describes the actions planned in response to the recommendations.

Recommendation 1: Provide a point of contact to the Under Secretary of Defense (Comptroller) for the financial reporting issues working group recommended in our (DoDIG's) previous report.

The point of contact is Ms. Mary Lou Stokes, DSWA Comptroller. Her name was provided to the working group point of contact, Mr. D. Ritchie, OSD Comptroller (Policy) on 21 October 1997.

Recommendation 2: Identify the systems that include Government property in the custody of contractors, determine whether that information is included in data reported for the financial statements, and report the information to their agency Comptrollers and the DoD Chief Financial Officer.

Through the audit, the system identified that included Government property in the custody of contractors for DSWA is Contract Property Management System (CPMS). Currently, the information cannot be included in data reported for the financial statements. This has previously been identified by DSWA as a material weakness in its annual Statement of Assurance. DSWA will work with the OSD working group to resolve this DoD systemic problem.

The point of contact for this report is CAPT Phil Crowell, DSWA Inspector General, (703) 325-7096. Thank you for the opportunity to respond to this audit report.

A handwritten signature in black ink, appearing to read "Gary L. Curtin".

GARY L. CURTIN
Major General, USAF
Director

American Forces Information Service Comments



DEPARTMENT OF DEFENSE
AMERICAN FORCES INFORMATION SERVICE
601 NORTH FAIRFAX STREET
ALEXANDRIA, VIRGINIA 22314-2007

OCT 23 1997

Operating
elements

MEMORANDUM FOR THE ASSISTANT INSPECTOR GENERAL FOR AUDITING,
DOD

Armed Forces
Radio and
Television
Service

SUBJECT: Draft Audit Report by Selected Defense Agencies of
Government Property in the Custody of Contractors
(Project No. 6FI-2009.01)

Broadcast
Center

American Forces Information Service (AFIS) comments on the
findings and recommendations in the subject draft report are
forwarded in accordance with DoD IG memorandum of August 21,
1997.

Defense
Visual
Information

Financial Reporting of Government Property

Joint
Combat
Camera
Center

1. **FINDING:** The AFIS, DISA, and DSWA did not report
Government property in the FY 1996 financial statements in
accordance with financial reporting requirements.

Defense
Visual
Information
Center

RECOMMENDATION 1: Provide a point of contact to the Under
Secretary of Defense (Comptroller) for the financial reporting
issues working group recommended in our previous report.

Defense
Information
Schools

COMMENT: Concur. AFIS financial reporting issues working
group points of contact were provided to the applicable action
officer in the Office of the Under Secretary of Defense
(Comptroller) October 22, 1997, however, AFIS was informed by
the action officer that the Comptroller has not yet approved
the above recommendation and the recommended working group may
never be formed.

Print
Media

Current News
Analysis and
Research
Service

Stars and
Stripes
Overlight

RECOMMENDATION 2: Identify the systems that include
Government property in the custody of contractors, determine
whether that information is included in data reported for the
financial statements, and report the information to their
agency Comptrollers and the DoD Chief Financial Officer.

Television
Audio
Support
Activity

Office of the Assistant Secretary of Defense (Public Affairs)

American Forces Information Service Comments

COMMENT: Partially-concur. AFIS property, to include Government property in the custody of contractors, is maintained on the Defense Property Accountability System (DPAS). DPAS is the system AFIS and its subordinate activities use to account for property.

Presently, AFIS is required by the Defense Finance and Accounting Service Indianapolis Center's (DFAS-IN) memo dated August 14, 1996, subject: Certification of Fiscal Year-End General Ledger Account Balances for Property by Accountable Property Officers--TI 97 Reporting, to certify on a quarterly basis the accuracy of amounts reported for real property, equipment and inventory on feeder reports used in preparing fiscal year-end financial reports. AFIS believed this quarterly reporting and certifying would be used to provide property value information for the financial statement. However, in September 1997, AFIS learned through information provided by the Washington Headquarters Services (WHS) Finance and Accounting Office that the data being provided on a quarterly basis to DFAS-IN was not being reported anywhere. Based on that information and the lack of clear financial reporting guidance from any of the servicing DFAS centers, AFIS has good reason to believe the only assets reported in the FY 97 financial statement are those collected by WHS for AFIS HQ, and then only representing capital investment equipment. Because of this lack of clear financial reporting guidance from DFAS, AFIS is in the process of working out the details of how the property information will be collected, reported, and placed onto each field activity's trial balance for inclusion in future AFIS financial statements.

Finally, AFIS has reported this information to its responsible agency official, and will pursue resolution of this latest obstacle. AFIS will provide the property information to the DoD CFO when the financial reporting issues working group convenes.

Management Control Program

2. **FINDING:** Adequacy of Management Controls. Controls were not in place to ensure Government property in the custody of contractors was accounted for and reported in the financial statements.

COMMENT: Partially concur. AFIS has 100% accountability for all Government property in the custody of contractors,

American Forces Information Service Comments

however, prior to FY 97 AFIS was unaware of the requirement to ensure that Government property in the custody of contractors was reported on the financial statement. AFIS has had little guidance from the servicing DFAS centers, and now, based on the information discussed at recommendation #2, AFIS will go to each servicing DFAS center to determine how to report this information for inclusion to each AFIS activity's trial balance.

3. FINDING: Adequacy of Management's Self-Evaluations. Officials at AFIS and DISA did not identify financial reporting of Government property as an assessable unit and, therefore, did not identify or report the material management control weakness identified by the audit.

COMMENT: Partially concur. Neither OMB Circular A-130 nor DoD Directive 5010.38, "Management Control (MC) Program," require that financial reporting of Government property be identified as separate assessable unit. Financial reporting of Government property will be incorporated into both the Logistics and Budget & Finance assessable units and will be reviewed accordingly. This review process, in addition to the previously mentioned recommendations and corresponding responses, will be used to identify problems with financial reporting of Government property for timely correction. AFIS has reported this weakness in Tab A of the FY 97 Statement of Assurance.

Please direct any questions to CPT Stepanchuk, (703)428-0715, DSN 328-0715.

Col Jordan E. Rizer, USA
Col Jordan E. Rizer
Director

Audit Team Members

This report was prepared by the Finance and Accounting Directorate, Office of the Assistant Inspector General for Auditing, DoD.

F. Jay Lane
Richard B. Bird
Linda A. Pierce
Amy J. Frontz
Lisa A. Ramseyer
William E. Hosick
Deborah Curry

INTERNET DOCUMENT INFORMATION FORM

A . Report Title: Financial Reporting by Selected Defense Agencies of Government Property in the Custody of Contractors

B. DATE Report Downloaded From the Internet: 09/27/99

C. Report's Point of Contact: (Name, Organization, Address, Office Symbol, & Ph #):
OAIG-AUD (ATTN: AFTS Audit Suggestions)
Inspector General, Department of Defense
400 Army Navy Drive (Room 801)
Arlington, VA 22202-2884

D. Currently Applicable Classification Level: Unclassified

E. Distribution Statement A: Approved for Public Release

F. The foregoing information was compiled and provided by:
DTIC-OCA, Initials: __VM__ Preparation Date 09/27/99

The foregoing information should exactly correspond to the Title, Report Number, and the Date on the accompanying report document. If there are mismatches, or other questions, contact the above OCA Representative for resolution.