

Audit



Report

OFFICE OF THE INSPECTOR GENERAL

**MATERIAL ACCOUNTING AND MANAGEMENT
CONTROL WEAKNESSES IN THE DEFENSE AGENCIES'
FYS 1995 AND 1996 FINANCIAL INFORMATION**

Report No. 97-110

March 17, 1997

19991026 061

DTIC QUALITY INSPECTED 4

Department of Defense

DISTRIBUTION STATEMENT A
Approved for Public Release
Distribution Unlimited

ARIC-01-0177

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) 604-8939 (DSN 664-8939) or FAX (703) 604-8932. Ideas and requests can also be mailed to:

OAIG-AUD (ATTN: APTS Audit Suggestions)
Inspector General, Department of Defense
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 to the Defense Hotline, The Pentagon, Washington, D.C. 20301-1900. The identity of each writer and caller is fully protected.

Acronyms

DARPA	Defense Advanced Research Projects Agency
DFAS	Defense Finance and Accounting Service
DAO/WHs	Defense Accounting Office, Washington Headquarters Services
DIA	Defense Intelligence Agency
DISA	Defense Information Systems Agency
DLA	Defense Logistics Agency
DMA	Defense Mapping Agency
DSWA	Defense Special Weapons Agency
DTSA	Defense Technology Security Administration
KAR	Key Accounting Requirement
NSA	National Security Agency
OCHAMPUS	Office of the Civilian Health and Medical Program of the Uniformed Services
WHs	Washington Headquarters Services



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



March 17, 1997

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING
SERVICE

SUBJECT: Audit Report on Material Accounting and Management Control
Weaknesses in the Defense Agencies' FYs 1995 and 1996 Financial
Information (Report No. 97-110)

We are providing this summary report for information and use. Comments from the DoD Education Activity on a draft of this report were considered in preparing the final report.

The report summarizes accounting system weaknesses identified during audits of Defense agencies' FYs 1995 and 1996 financial data. The audits were made of the DoD-wide appropriations (Department 97), which are allocated to 15 Defense agencies, 9 DoD field activities, and 16 other DoD organizations. For the purposes of this report, the term "Defense agencies" includes Defense agencies, DoD field activities, and other Defense organizations. The report also summarizes the status of corrective actions taken by Defense agencies to correct accounting system weaknesses identified during audits of Defense agencies' FY 1994 financial statements. Those accounting system weaknesses were summarized in Inspector General, DoD, Report No. 97-008, "Summary Report on the FY 1994 Financial Statement Audits of Defense Agencies," October 25, 1996.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Ms. Mary Lu Ugone, Audit Program Director, at (703) 604-9529 (DSN 664-9529) or Mr. Karim Malek, at (703) 604-9554 (DSN 664-9554). See Appendix O for the report distribution. The audit team members are listed inside the back cover.

David K. Steensma

David K. Steensma
Deputy Assistant Inspector General
for Auditing

Office of the Inspector General, DoD

Report No. 97-110
(Project No. 6RA-2014.03)

March 17, 1997

Material Accounting and Management Control Weaknesses in the Defense Agencies' FYs 1995 and 1996 Financial Information

Executive Summary

Introduction. This report summarizes accounting system and management control weaknesses identified during audits of Defense agencies'¹ FYs 1995 and 1996 financial data. The audits were made of the DoD-wide appropriations (Department 97²), which are allocated to 15 Defense agencies, 9 DoD field activities, and 16 other DoD organizations. For FYs 1995 and 1996, DoD-wide appropriations were \$37 billion and \$39 billion, respectively. The report also summarizes the status of corrective actions taken by Defense agencies to correct accounting system weaknesses identified during audits of Defense agencies' FY 1994 financial statements. The weaknesses were summarized in Inspector General, DoD, Report No. 97-008, "Summary Report on the FY 1994 Financial Statement Audits of Defense Agencies," October 25, 1996.

This report also discusses recent DoD financial management initiatives designed to improve Defense agency financial and financial-related information.

Audit Objectives. The primary audit objective was to summarize Defense agency accounting system weaknesses and related management control program weaknesses identified during audits of defense agencies' FYs 1995 and 1996 financial data. We also summarized the status of corrective actions taken by Defense agencies to correct accounting system weaknesses identified during audits of Defense agencies' FY 1994 financial statements.

Audit Results. Defense agency accounting system weaknesses for FYs 1995 and 1996 were primarily related to four key accounting requirements:

- o general ledger control and financial reporting,
- o property and inventory accounting,
- o system controls (fund and internal), and
- o accrual accounting.

Defense agency accounting system had weaknesses in six additional key accounting requirements: accounting for receivables, including advances; audit trails; cash procedures and accounts payable; system documentation; system operations; and user

¹For the purposes of this report, the term "Defense agencies" includes Defense agencies, DoD field activities, and other Defense organizations.

²The Department of the Treasury uses department code "97" to identify general fund appropriations for the Office of the Secretary of Defense.

information needs. Appendix G shows the specific accounting system weaknesses by Defense agency. Also identified were management control program weaknesses at nine Defense agencies. Consequently, general ledger account data were not reliable and may adversely affect the reliability of Defense agency financial statements.

The Defense agencies took aggressive actions to correct certain FY 1994 material accounting system and management control weaknesses (see Appendix L). (The synopses of FY 1994 Financial Statement Reports and Related Audit Reports is in Appendix F.) However, actions to correct other weaknesses were in process, not started, or may not be completed until FY 1998 to FY 2000 at the earliest (see Appendixes M and N).

The DoD management improvement initiatives will significantly improve the reliability of financial and related information. However, several initiative implementation dates have slipped, and key initiatives need to be tested and implemented to fully measure their success.

Management Comments. The Department of Defense Education Activity commented and disagreed that Antideficiency Act violations could have occurred because it had procurement funds to cover accounting adjustments. Further, the report did not show actions that were taken or under way to improve property accountability and the management control environment. See Part I for a discussion of management's comments and Part III for the complete text of the comments.

Audit Response. We revised the report and incorporated additional information to more clearly present the Department of Defense Education Activity problems and corrective actions.

Table of Contents

Executive Summary

Part I - Audit Results

Audit Background	2
Audit Objectives	2
Accounting and Management Control Weaknesses	3

Part II - Additional Information

Appendix A. Audit Process	14
Scope and Methodology	14
Prior Audits and Other Reviews	17
Appendix B. Key Accounting Requirements	18
Appendix C. Synopsis of FYs 1995 and 1996 Defense Agency Financial Statement Reports and Related Audit Reports	20
Appendix D. Management Control Programs	30
Appendix E. Defense Agencies Audited	37
Appendix F. Synopses of FY 1994 Financial Statement Reports and Related Audit Reports	38
Appendix G. Accounting System Weaknesses at the Defense Agencies	42
Appendix H. General Ledger Control and Financial Reporting Weaknesses (KAR 1)	44
Appendix I. Property and Inventory Accounting Weaknesses (KAR 2)	48
Appendix J. Accrual Accounting (KAR 5)	52
Appendix K. System Controls (Fund and Internal) (KAR 7)	53
Appendix L. Correction of Material Accounting System Weaknesses	55
Appendix M. Previously Reported Material Accounting System Weaknesses Requiring Correction	59
Appendix N. DoD Initiatives	62
Appendix O. Report Distribution	64

Part III - Management Comments

Department of Defense Education Activity Comments	68
---	----

Part I - Audit Results

Audit Background

The Chief Financial Officers Act of 1990 (Public Law 101-576) established requirements for Federal organizations to submit audited financial statements to the Director, Office of Management and Budget. Public Law 103-356, "Federal Financial Management Act of 1994," significantly expanded the audit requirements established in the Chief Financial Officers Act. The law requires the Inspectors General to audit consolidated financial statements covering all accounts and activities for FY 1996 and each succeeding year.

The DoD-wide financial statements includes a funds category entitled, "Other Defense Organizations." In support of the FY 1996 consolidated financial statement audit, we audited management controls and compliance with financial regulations for those organizations included in the Other Defense Organizations category. Although we do not plan to render an audit opinion on Other Defense Organizations, information gathered on the Defense agencies will be subject to analytical review in order to render an opinion on the overall DoD-wide financial statements.

DoD 7000.14-R, "Financial Management Regulation," volume 1, chapter 3, May 1993, provides specific DoD policies for evaluating accounting systems. The Regulation specifies 13 key accounting requirements (KARs) with which accounting systems must comply. The Regulation further states that a material noncompliance with a KAR requires corrective action within a reasonable period. The KARs are a composite of requirements of the General Accounting Office, Office of Management and Budget, Department of the Treasury, and DoD (see Appendix B).

Audit Objectives

The primary audit objective was to summarize Defense agency¹ accounting system and related management control program weaknesses identified during audits of Defense agencies' FYs 1995 and 1996 financial data (see Appendix C). Management control programs are discussed in Appendix D.

See Appendix A for a discussion of the audit process and the KARs reviewed at the 31 Defense agencies and Appendix E for a list of Defense agencies reviewed.

As shown in Appendix L, we also summarized the status of corrective actions taken by Defense agencies to correct accounting weaknesses identified during audits of Defense agencies' FY 1994 financial statements. Appendix F has synopses of FY 1994 financial statement reports and related audit reports.

¹For the purposes of this report, the term "Defense agencies" includes Defense agencies, DoD field activities, and other Defense organizations.

Accounting and Management Control Weaknesses

The audits performed at the Defense agencies showed that accounting system weaknesses were primarily related to four KARs:

- o general ledger control and financial reporting (KAR 1) weaknesses at the accounting offices that support 22 Defense agencies;

- o property and inventory accounting (KAR 2) weaknesses at 9 Defense agencies;

- o accrual accounting (KAR 5) weaknesses at 3 Defense agencies;

and

- o system controls (fund and internal) (KAR 7) weaknesses at 5 Defense agencies.

The audits identified weaknesses in six additional KARs: accounting for receivables, including advances (three agencies); audit trails (one agency); cash procedures and accounts payable (three agencies); system documentation (one agency); system operations (one agency); and user information needs (one agency). The audits also identified related management control weaknesses at nine Defense agencies.

The Defense agencies have taken actions to correct certain material accounting system and management control weaknesses summarized in Inspector General, DoD, Report No. 97-008, "Summary Report on the FY 1994 Financial Statement Audits of Defense Agencies," October 25, 1996. However, other actions to correct certain weaknesses were in process, not started, or may not be completed until FY 1998 at the earliest.

As a result, general ledger account data at the Defense agencies were not reliable and the financial information for FYs 1995 and 1996 is of limited use.

Accounting System Weaknesses

For FYs 1995 and 1996 financial information on the 31 Defense agencies, we identified material and other accounting system weaknesses related to 10 KARs. Discussion of the 10 KARs follows, and Appendix G identifies KAR weaknesses at the specific Defense agencies.

General Ledger Control and Financial Reporting (KAR 1). The KAR 1 states that an accounting system must have general ledger control and maintain a DoD approved general ledger account structure for all categories of budgetary

Accounting and Management Control Weaknesses

and proprietary accounts. In addition, the system must provide full financial disclosure, accountability, and reports for management purposes and for necessary external reporting to the Office of Management and Budget and the Department of the Treasury.

Material general ledger control and financial reporting weaknesses existed at the accounting offices that support 22 Defense agencies. Generally, the Defense agencies or their supporting accounting offices inappropriately used budget execution reports rather than accounts listed in the general ledger as the data source for financial statements. Also, Defense agencies or their accounting offices did not maintain subsidiary ledgers for general ledger accounts, did not make adjusting or closing entries, omitted pertinent financial information from trial balances, and did not have a complete general ledger control system in place over Defense agency appropriations. Those weaknesses existed because financial personnel did not correctly program financial systems to process trial balances, the accounting systems used to process financial data did not have the necessary capabilities, the accounting offices submitted incomplete trial balances, and the Defense agencies and accounting offices did not reconcile general ledger accounts with supporting subsidiary accounts. Details on the material weaknesses related to KAR 1 are in Appendix H.

Property and Inventory Accounting (KAR 2). The KAR 2 states that an accounting system must account, in quantitative and monetary terms, for the procurement, receipt, issue, and control of plant property, equipment, inventory, and material. The property management system must include accounting controls over inventory ledgers that identify the item, its location, quantity, acquisition date, cost, and other information. Physical controls include periodically reconciling physical inventories to the accounting records.

Material property and inventory weaknesses existed at the Army National Guard, Defense Advanced Research Projects Agency, Defense Intelligence Agency (DIA), Defense Logistics Agency (DLA), Defense Technology Security Administration (DTSA), Department of Defense Education Activity, National Security Agency (NSA), Office of the Civilian Health and Medical Program of the Uniformed Services (OCHAMPUS), and Office of the Secretary of Defense. Material property and inventory weaknesses occurred primarily because Defense agencies:

- o capitalized² military equipment acquisitions that should have been expensed,
- o did not maintain complete and accurate property records,
- o did not reconcile general ledger account balances with subsidiary property records, and

²Property purchased is "capitalized" when it is recorded as an asset in financial accounting records. The cost of property not capitalized is recorded as a current operating expense. (Current capitalization threshold is \$100,000.)

o either did not report or duplicated reporting of military equipment acquisitions.

As a result, property, equipment, and inventory account balances shown in general and subsidiary ledgers were materially incomplete and inaccurate and thus were not reliable for financial reporting purposes. Details on the Defense agencies' material and other weaknesses related to KAR 2 are in Appendix I.

Accounting for Receivables Including Advances (KAR 3). An accounting system must accurately and promptly account for all accounts receivable (all debts to the U.S. Government) to provide timely and reliable financial status. Accounts receivable shall be reduced upon collection of funds, and uncollectible amounts should be promptly written off. Also, advances shall be recorded as assets until receipt of the goods or services. Accounting control must be maintained over advances made to employees, and advances must be promptly recorded and reconciled to general ledger control accounts.

Material accounting weaknesses regarding receivables existed at DIA, NSA, and the OCHAMPUS. The DIA incorrectly recognized completion of reimbursable work prior to the completion of the work. Also, DIA did not record checks received for reimbursable work performed at the DIA and did not promptly review and reconcile outstanding travel advances or correctly record travel advance settlements. The NSA did not reconcile differences between account balances shown in the consolidated general ledger and supporting subsidiary ledgers for accounts receivables and advances.

OCHAMPUS accounting staff did not record the proper accounting transaction for an undetermined amount paid to and due back from contractors. When OCHAMPUS issued a contract modification that decreased the amount to be paid to a contractor, OCHAMPUS recorded a negative accounts payable instead of establishing a refunds receivable for the funds a contractor owed. As a result, receivables were understated by an undetermined amount.

Accrual Accounting (KAR 5). Accrual accounting must recognize accountable transactions or events as they occur. Transactions may be recorded in accounting records as they occur or be adjusted monthly to the accrual basis. Amounts of accrued expenditures and revenues must be recorded only when supported by prescribed documentary evidence on the basis of initial documentation received.

Material accrual accounting weaknesses existed at DIA, NSA, and OCHAMPUS. DIA and NSA used an accounting system that did not accrue liabilities until disbursements were recorded. The OCHAMPUS did not accrue liabilities because it did not have enough personnel to accomplish accrual tasks. See Appendix J for additional discussion of matters related to KAR 5.

es

Audit Trails (KAR 8). The financial transactions on accounting system processes must be adequately supported with pertinent source documents. Audit trails should allow a transaction to be traced from initiation through processing to final reports.

We identified material KAR 8 weaknesses related to the DFAS Columbus Center, which prepares the financial statements for the DLA General Fund appropriations. The DFAS Columbus Center uses the Defense Business Management System to record, analyze, process, and report DLA General Fund transactions. That system did not have the capability to research and correct an imbalance between general and subsidiary ledgers and between proprietary and budgetary equivalents. Also, the Defense Business Management System did not allow the reconciliation of trial balances at the agency organizational level.

In addition, the DFAS Columbus Center had not attempted to reconcile the DLA General Fund appropriation trial balance to subsidiary ledgers and did not have supporting documentation for \$18 million of the \$65 million in receivables reported in the subsidiary ledger.

Cash Procedures and Accounts Payable (KAR 9). An accounting system shall be designed to verify timely payments based on properly approved disbursement documents. Payment procedures must comply with the Prompt Payment Act, and accounts payable should be recorded when goods or services are received.

Material weaknesses related to KAR 9 existed at the Army National Guard, the DIA, and the OCHAMPUS. The Army National Guard did not record accounts payable upon evidence of receipt of equipment and recorded accounts payable for transactions that did not establish Government liabilities. The Army National Guard was unable to record liabilities upon receipt of equipment because accounting officials did not receive evidence to support the transactions. Also, the Army National Guard recorded \$5.1 million of liabilities that were, in fact, disbursements. Army National Guard officials were aware of the incorrect recording of accounts payables in the general ledger, but did not correct account balances because of other priorities.

The DIA did not promptly record disbursements by others transactions and as of June 30, 1996, DIA had disbursements of:

- o \$114.0 million in disbursement vouchers awaiting processing;
- o \$87.9 million of disbursements in transit; and
- o \$20.6 million of unreconciled differences in disbursements in transit.

As a result, the financial information produced and reported by DIA cannot be relied on to prepare required financial statements.

OCHAMPUS did not comply with the Prompt Payment Act because payment procedures did not always permit OCHAMPUS to make timely payments or to record and make required interest payments. OCHAMPUS paid \$70,591 in

February 1995 in interest charges due to late payments. OCHAMPUS personnel stated that after February 1995, they corrected the late payment problem by implementing new payment procedures. However, written procedures were not available from the accounting staff, and in June 1995, OCHAMPUS paid another \$24,796 in interest charges when the accounting staff did not promptly process 19 contract modifications.

System Documentation (KAR 10). The accounting system must have adequate system documentation, including documented interfaces between accounting system segments. The DFAS Indianapolis Center provides finance and accounting support to the Army and the Defense agencies. The DFAS Indianapolis Center uses the Federal Financial System (previously the General Ledger Accounting and Report System) to receive, adjust, and consolidate the general ledger trial balances from reporting fiscal stations.

The DFAS Indianapolis Center process of receiving, adjusting, and consolidating the general ledger trial balances from fiscal stations was not documented. The DFAS Indianapolis Center did not prepare a required narrative description of the Federal Financial System to demonstrate the system's conceptual processes and procedures to system users, auditors, and evaluators. In addition, the DFAS Indianapolis Center did not document:

- o the flow of financial data through the Federal Financial System and
- o lists and descriptions of
 - the edit tables that are used to validate the integrity of the financial data on the general ledger trial balances submitted by fiscal stations,
 - the types of adjusting entries made to the general ledger trial balances submitted by the fiscal stations, and
 - the process for making adjusting entries.

The DFAS Indianapolis Center also did not document:

- o a table showing the Defense agencies and appropriations that should be reported in "Other Defense Organizations" in the FY 1996 consolidated financial statements; or
- o descriptions of
 - system interfaces with other financial systems,
 - internal controls and safeguards, and
 - the process for consolidating the general ledger trial balances reported by fiscal stations for Department 97 appropriations on the financial statements; and

o examples of source documents used and outputs and reports generated by the Federal Financial System.

System Operations (KAR 11). The accounting system operations shall be adequately planned and organized to assure that financial management and accounting objectives are met in an economical and efficient manner. OCHAMPUS had a material KAR 11 weaknesses because OCHAMPUS did not have written procedures for preparing reportable financial data and because OCHAMPUS staff did not follow DoD guidance for deriving financial information for the DFAS Indianapolis Center.

User Information Needs (KAR 12) at the Office of the Civilian Health and Medical Program of the Uniformed Services. The KAR 12 states that user information needs and requirements as to quality, accuracy, timeliness, reliability, and responsiveness of an accounting system shall be adequate in response to program managers, financial managers, and other users. Further, the accounting system shall satisfy users as to their reporting requirements particularly regarding month-end reports.

The OCHAMPUS financial records were not reliable, and OCHAMPUS officials could not use them to verify the availability of funds for the reimbursable program. Also, the FY 1995 OCHAMPUS financial records did not provide assurance that management did not obligate funds in excess of the authorized reimbursable program.

Management Control Weaknesses

Management control weaknesses, as defined by DoD Directive 5010.38, existed at the DFAS Cleveland, Columbus, and Indianapolis Centers; DTSA; DIA; Army National Guard; NSA; Defense Advanced Research Projects Agency; OCHAMPUS; DLA; Department of Defense Education Activity; and the Army Reserves. The weaknesses at each agency are discussed in Appendix D.

Correction of Previously Reported Material Accounting System Weaknesses

The Defense agencies have taken aggressive actions to correct material accounting system weaknesses identified during audits of Defense agencies' FY 1994 financial statements; however, significant weaknesses remain. Appendix L shows the status of corrective actions taken by Defense agencies in response to accounting system weaknesses. Defense agencies took the following actions to correct previously reported material accounting system weaknesses:

Accounting and Management Control Weaknesses

- o made accounting entries to correct erroneous general ledger transactions,

- o reconciled accounting records to subsidiary records and made appropriate adjusting entries,

- o established procedures to ensure more reliable subsidiary property records,

- o implemented training programs to ensure that employees performing accounting functions are provided technical instruction, and

- o analyzed or planned to analyze military equipment transactions to determine whether acquisitions should have been capitalized or expensed.

Despite those improvements, Defense agencies were not able to initiate timely actions to correct other material internal control weaknesses. Appendix M, which discusses the uncorrected weaknesses, indicates that Defense agencies:

- o continue to inappropriately use budget execution reports to prepare financial statements rather than use accounts in the general ledger, which should contain sufficient financial information to prepare complete and accurate financial statements;

- o have not integrated property systems and accounting systems and, therefore, controls are often not adequate to ensure that general ledger control accounts agree with subsidiary accounts;

- o did not establish continuing education programs to ensure that employees maintain necessary skills to prepare agency financial statements; and

- o have not performed periodic inventories of agency products and have not valued the products.

DoD Financial Management Initiatives

The DoD has developed several financial management improvement initiatives to significantly improve the reliability and integrity of financial and related information. The initiatives include the Program Budget and Accounting System, the DoD Property Accountability System, Chief Financial Officer financial statements, standard finance and accounting systems, and consolidation of DoD accounting offices. However, several initiative implementation dates have slipped, and key initiatives need to be tested and implemented to fully measure their success. The initiatives are discussed in more detail in Appendix N.

Conclusion

The Defense agencies' financial information for FYs 1995 and 1996 is of limited use. The audits identified material weaknesses related to KARs at 31 Defense agencies. The Defense agencies have taken aggressive actions to correct material accounting system weaknesses identified during audits of Defense agencies' FY 1994 financial information; however, significant weaknesses remain. DoD financial management improvement initiatives will improve Defense agency compliance with KARs.

Management Comments and Audit Response

Management Comments. The Department of Defense Education Activity provided comments on the draft of this summary report. The Department of Defense Education Activity disagreed that Antideficiency Act violations could have occurred as summarized for Inspector General, DoD, Report No. 97-078, "Report on Potential Antideficiency Act Violations at the Department of Defense Education Activity," January 23, 1997. The Department of Defense Education Activity also disagreed with terminology in Report No. 97-078 regarding local area networks. The Department of Defense Education Activity also commented that the summary report did not provide management actions that were taken or under way in response to recommendations in Inspector General, DoD, Report No. 97-082, "Property Accountability for the Department of Defense Education Activity," January 28, 1997 or reflect the corrective actions taken in response to Inspector General, DoD, Report No. 96-181, "Management Control Environment for the Department of Defense Education Activity," June 28, 1996. Each of the reports and issues is discussed in Appendix C. See Part III for the complete text of the comments.

Audit Response. In response to management comments, we incorporated additional information in Appendix C regarding Report Nos. 97-078 and 97-082. Also, we added information on Department of Defense Education Activity corrective actions taken in response to Report No. 96-181

This page was left out of original document

Part II - Additional Information

Appendix A. Audit Process

Scope and Methodology

This report summarizes accounting system and applicable management control program weaknesses identified during audits of Defense agencies' FYs 1995 and 1996 financial information. We reviewed and summarized material weaknesses discussed in 17 audit reports issued from August through December 1996. Appendix E lists the Defense agencies that were audited during that period.

In addition, we summarized the status of corrective actions taken by Defense agencies in response to accounting system weaknesses identified during audits of Defense agencies' FY 1994 financial statements. Inspector General, DoD, Report No. 97-008, "Summary Report on the FY 1994 Financial Statement Audits of Defense Agencies," October 25, 1996, includes a list of applicable Defense agencies.

Limitations to Audit Scope. The audits did not review compliance with each of the 13 KARs at all 31 Defense agencies. The audits also did not review financial information for the DFAS Cleveland, Columbus, Denver, and Indianapolis Centers, but reviewed the process the centers used to obtain and report on Defense agencies' FYs 1995 and 1996 financial information. The table on the following page summarizes the KARs we reviewed.

Based on preliminary reviews of Defense agency financial and accounting systems, our initial audit approach has focused on the adequacy of Defense agency management control programs and compliance with selected KARs. Audits of management control programs include evaluating the implementation of controls and the performance of annual accounting system reviews. Evaluating compliance with selected KARs includes evaluating compliance with KARs that have significant application to Defense agencies.

Audit Period and Standards. We performed this financial-related audit from October through December 1996 in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD. We did not rely on computer-processed data or statistical sampling procedures to prepare this summary report.

Summary of KARs Reviewed at Defense Agencies

KAR	1	2	3	4	5	6	7	8	9	10	11	12	13
Agency													
AFIS	P/R	-	-	-	-	-	-	-	-	-	-	-	-
ARMYRES	R	P/R	-	-	-	-	P/R	P/R	-	P/R	-	-	P/R
ARNG	R	P/R	-	-	-	-	P/R	-	P/R	-	-	-	-
BMDO	P/R	-	-	-	-	-	-	-	-	-	-	-	-
CIM	P/R	-	-	-	-	-	P/R	P/R	-	P/R	P/R	-	-
CIO	P/R	-	-	-	-	-	-	-	-	-	-	-	-
DARPA	P/R	P/R	-	-	-	-	P/R	P/R	-	P/R	-	-	P/R
DAU	P/R	-	-	-	-	-	-	-	-	-	-	-	-
DCAA	P/R	-	-	-	-	-	-	-	-	-	-	-	-
DIA	R	R	R	-	R	P/R	P/R	R	R	P/R	P/R	P/R	P/R
DIS	P/R	-	-	-	-	-	-	-	-	-	-	-	-
DISA	P/R	P/R	-	-	-	-	-	-	-	-	-	-	-
DLA	P/R	P/R	-	-	-	-	P/R	-	-	-	-	-	-
DLSA	P/R	-	-	-	-	-	-	-	-	-	-	-	-
DMA	R	R	-	R	P/R	-	P/R	P/R	P/R	P/R	P/R	P/R	P/R
DMPA	P/R	-	-	-	-	-	-	-	-	-	-	-	-
DoDEA	R	R	R	-	-	-	R	R	-	R	R	R	R
DSWA	R	R	P/R	-	P/R	P/R	P/R	R	P/R	R	P/R	P/R	P/R
DTSA	P/R	P/R	-	-	-	-	P/R	P/R	-	P/R	P/R	-	-
FEMP	P/R	-	-	-	-	-	-	-	-	-	-	-	-
IG	P/R	-	-	-	-	-	-	-	-	-	-	-	-
JS	P/R	-	-	-	-	-	-	-	-	-	-	-	-
NSA	R	R	R	-	R	P/R	P/R	P/R	R	R	P/R	P/R	P/R
OCHAMPUS	R	R	R	-	R	R	R	R	R	P/R	P/R	P/R	R

Additional Defense agencies, the legend, and a list of acronyms are listed on the following page.

Summary of KARs Reviewed at Defense Agencies (Cont'd)

KAR	1	2	3	4	5	6	7	8	9	10	11	12	13
Agency													
OEA	P/R	--	--	--	--	--	--	--	--	--	--	--	--
OSD	P/R	--	--	--	--	--	--	--	--	--	--	--	--
OSIA	P/R	--	--	--	--	--	--	--	--	--	--	--	--
POW/MIA	P/R	--	--	--	--	--	--	--	--	--	--	--	--
SOC	P/R	--	--	--	--	--	--	--	--	--	--	--	--
USUHS	P/R	--	--	--	--	--	--	--	--	--	--	--	--
WHS	P/R	P/R	--	--	--	--	P/R	P/R	--	P/R	P/R	--	--

R Reviewed
P/R Partially Reviewed
-- Not Reviewed

Acronyms

AFIS American Forces Information Service
ARMYRES Army Reserves
ARNG Army National Guard
BMDO Ballistic Missile Defense Organization
CIM Corporate Information Management
CIO Central Imagery Office (now National Imagery and Mapping Agency)
DARPA Defense Advanced Research Projects Agency
DAU Defense Acquisition University
DCAA Defense Contract Audit Agency
DLSA Defense Legal Services Agency
DIS Defense Investigative Service
DISA Defense Information Systems Agency
DMIPA Defense Medical Program Activity
DoDEA DoD Education Activity
FEMP Federal Energy Management Program
IG Inspector General
JS Joint Staff
OEA Office of Economic Adjustment
OSD Office of the Secretary of Defense
OSIA Off-Site Inspection Agency
POW/MIA Defense Prisoner of War/Missing in Action Office
SOC Special Operations Command
USUHS Uniformed Services University of the Health Sciences

Audit Contacts. During the audits, we visited or contacted individuals and organizations within the 31 Defense agencies (see Appendix E).

Prior Audits and Other Reviews

From August 1996 through January 1997, we issued 17 audit reports (see Appendix C) on Defense agencies' FYs 1995 and 1996 financial statements.

Also, on October 25, 1996, we issued Inspector General, DoD, Report No. 97-008, "Summary Report on the FY 1994 Financial Statement Audits of Defense Agencies." Report No. 97-008 summarizes accounting system and management control weaknesses identified during research and audits of Defense agencies' FY 1994 financial statements. Appendix F includes a synopsis of each of the audit reports summarized in Report No. 97-008.

Appendix B. Key Accounting Requirements

The 13 key accounting requirements (KARs) are included in DoD 7000.14-R, "Financial Management Regulation," volume 1, chapter 3, May 1993. The following is a brief description of each KAR.

KAR 1, General Ledger Control and Financial Reporting. The accounting system must have general ledger control and maintain a DoD approved general ledger account structure for assets, liabilities, equity, expenses, losses, gains, transfers in and out, and financing sources. In addition, full financial disclosure, accountability, adequate financial information, and reports must be provided for management purposes and for necessary external reporting to the Office of Management and Budget and the Department of the Treasury.

KAR 2, Property and Inventory Accounting. The system must account in quantitative and monetary terms for the procurement, receipt, issue, and control of plant, property, equipment, inventory, and material. The property management system must include accounting controls over inventory ledgers that identify the item, its location, quantity, acquisition date, cost, and other information. Subsidiary property records are reconciled periodically to general ledger accounts.

KAR 3, Accounting for Receivables Including Advances. The system must account for all accounts receivable (all debts to the U.S. Government) accurately and promptly to provide timely and reliable financial status.

KAR 4, Cost Accounting. Cost accounting must involve accounting analysis and reporting on costs of production of goods or services or operation of programs, activities, functions, or organizational units. Cost accounting shall be provided in the accounting system if it is required in such instances as pricing decisions, productivity improvement decisions or measurement of performance.

KAR 5, Accrual Accounting. Accrual accounting must recognize the accountable aspects of financial transactions or events as they occur. Transactions may be recorded in accounting records as they occur or be adjusted to the accrual basis at each month's end. Unpaid personnel compensation and benefits that have been earned as of the end of the pay year must be accrued in full or in part. Accrued payroll for civilian and military salaries and wages, unfunded annual leave, and annual leave must be recorded and reconciled with the actual payroll.

KAR 6, Military and Civilian Payroll Procedures. Payroll systems must incorporate controls of payroll amounts and payroll deductions to ensure smooth payroll processing action and to minimize incorrect payments. Unpaid personnel compensation and benefits, including annual leave, that have been earned by employees as of the end of the pay year must be accrued in full. Personnel compensation and all employee benefit expenses shall be reported and disclosed in the financial statements.

KAR 7, System Controls (Fund and Internal). The accounting system must ensure that obligations and expenditures do not exceed the amount appropriated. The system must provide a process and procedures for control over errors. The system must show the appropriations and funds to be accounted for and a description of the accounting entity's proposed fund distribution and control process. The system must have good fund control procedures to prevent untimely liquidation of obligations, unmatched expenditures, and undistributed disbursements. The system must have adequate internal controls to prevent, detect, and correct errors and irregularities that occur throughout the system.

KAR 8, Audit Trails. The financial transactions on accounting system processes must be adequately supported with pertinent source documents. Audit trails should allow a transaction to be traced from initiation through processing to final reports.

KAR 9, Cash Procedures and Accounts Payable. The accounting system shall be designed to verify timely payments based on properly approved disbursement documents. Payment procedures must comply with the Prompt Payment Act. Accounts payable should be recorded when goods or services are received.

KAR 10, System Documentation. The accounting system must have adequate system documentation, including documented interfaces between accounting system segments.

KAR 11, System Operations. Accounting system operations shall be adequately planned and organized to assure that financial management and accounting objectives are met in an economical and efficient manner. There should be detailed system operating and maintenance procedures. Also, there should be periodic system reviews to assure that the system is functioning as intended.

KAR 12, User Information Needs. The accounting system must satisfy users' needs of quality, accuracy, timeliness, and reliability to facilitate management's decisionmaking process.

KAR 13, Budgetary Accounting. The accounting system shall support budget formulation and budget requests and shall control budget execution. Programming, budgeting, accounting, reporting classification, and coding structure should be uniform, mutually consistent, and synchronized with the organizational structure so that actual activity can be compared with enacted budgets to support future budget formulation for each activity.

Appendix C. Synopsis of FYs 1995 and 1996 Defense Agency Financial Statement Reports and Related Audit Reports

Inspector General, DoD, Report No. 97-082, "Property Accountability for the Department of Defense Education Activity," January 28, 1997. The report states that property records at the DoD Dependents Schools-Europe included property that did not exist and that property records were incomplete, inaccurate, and misvalued. The report estimated that \$30.3 million of \$110.7 million (acquisition value) of accountable property was either not located or not properly accounted for. The report recommends that the Department of Defense Education Activity direct supervisors to include appropriate comments on the control over property in the performance ratings of the DoD Dependents Schools-Europe Supply Branch personnel and the principals and establish management controls for physical inventories of property, new receipts, transfers, and acquisition cost of property and a written quality control program.

In addition, the report states that the DoD Dependents Schools-Europe Area Superintendent approved incomplete and inaccurate reports of survey for losses of accountable property. Consequently, the DoD Dependents Schools-Europe did not hold employees accountable for property losses totaling \$8.4 million processed in FY 1995. Also, the DoD Dependents Schools-Europe did not detect all or correct underlying system problems. The report recommends that the Department of Defense Education Activity establish management controls for investigating, processing, and approving reports of survey and designate a senior manager at Department of Defense Education Activity headquarters as approving authority for all reports of survey.

The report also states that controls in the Dependents Schools Automated Material Management System did not prevent:

- o data entry of zero dollar values or excessive dollar values for accountable property;
- o mass deletions of accountable property without supervisory approval or deletions without explanations;
- o incomplete input of accountable property record data base fields; and
- o duplicate property serial number recording for identical items.

The Dependents Schools Automated Material Management System lacked comprehensive edit checks and transaction user identification, and responsible personnel did not perform adequate quality assurance reviews on the data recorded in the system. As a result, DoD Dependents Schools-Europe accountable property was unaccounted for and approximately \$313,000 of duplicate work was performed. The report recommends that the Department of Defense Education Activity implement system changes to increase edit checks, identify the individual performing adjustments in the Dependents Schools

Appendix C. Synopsis of FYs 1995 and 1996 Defense Agency Financial Statement Reports and Related Audit Reports

Automated Material Management System, and eliminate the duplications of data entry. The report also recommends that the Department of Defense Education Activity establish quality assurance reviews and reassess staffing for the DoD Dependents Schools-Europe Supply Branch.

Finally, the report states that the Department of Defense Education Activity did not distribute the latest computer technology in an equitable manner and that some DoD Dependents Schools-Europe schools received unnecessary and unusable property. Accountable property was, therefore, susceptible to theft, and Department of Defense Education Activity students were not benefiting from the latest technology. The report recommends that the Department of Defense Education Activity develop a plan for managing property acquisitions and distributions. The Department of Defense Education Activity generally concurred with the recommendations and initiated responsive actions.

Inspector General, DoD, Report No. 97-079, "Documentation of the Federal Financial System Process at the Defense Finance and Accounting Service Indianapolis Center," January 24, 1997. The DFAS Indianapolis Center prepares financial statements for Defense agencies, including the Army Reserves portion of the National Guard and Reserve Equipment Appropriation. The DFAS Indianapolis Center did not document its process of receiving, adjusting, and consolidating the general ledger trial balances for the Department 97 appropriations from the Army Reserves' fiscal stations. Consequently, the FY 1995 Department 97 general ledger trial balances, which totaled \$37 billion for 30 Defense agencies, cannot be effectively tested. Without effective testing, auditors are unable to ensure the reliability of Department 97 financial statements required by the Chief Financial Officers Act of 1990 and the Federal Financial Management Act of 1994.

The report recommends that the DFAS Indianapolis Center document the process for receiving, adjusting, and consolidating the general ledger trial balances received from fiscal stations. The DFAS Indianapolis Center nonconcurred with the report recommendation and stated that Department 97 trial balances will be consolidated using an adequately documented new system, not the Federal Financial System. Additional management comments to describe the plan to document the processes used to produce consolidated financial statements were requested.

Inspector General, DoD, Report No. 97-078, "Report on Potential Antideficiency Act Violations at the Department of Defense Education Activity," January 23, 1997. The report states that the Domestic Dependent Elementary and Secondary Schools used \$6.9 million of FYs 1993 through 1996 appropriated Operation and Maintenance funds, rather than appropriated Procurement funds, to acquire and install investment items, including equipment and software for the local area network systems. Specifically, Domestic Dependent Elementary and Secondary Schools used \$5.4 million of Operation and Maintenance funds, \$662,882 of which was used in combination with \$775,849 of Procurement funds to acquire local area network equipment and software. Also, the DoD Dependents Schools used at least \$1.5 million of FYs 1994 through 1996 Operation and Maintenance funds, rather than Procurement funds, to procure and install local area networks. In addition, the

Appendix C. Synopsis of FYs 1995 and 1996 Defense Agency Financial Statement Reports and Related Audit Reports

aggregate cost of the local area networks acquired with Operation and Maintenance funds exceeded the dollar thresholds Congress established for the use of Operation and Maintenance. As a result, Antideficiency Act violations may have occurred.

The report recommends that the Under Secretary of Defense (Comptroller) direct the initiation of an investigation of potential Antideficiency Act violations if sufficient funds are not made available in the FYs 1993 through 1996 Procurement account to fund obligations made by the Director, Department of Defense Education Activity. The report also recommends that the Deputy Assistant Secretary of Defense (Personnel Support, Families, and Education) direct the Director, Department of Defense Education Activity, to investigate and report the potential Antideficiency Act violations based on the request of the Under Secretary of Defense (Comptroller) as outlined in DoD 7000.14-R, "Financial Management Regulation." In addition, the report recommends that the Director, Department of Defense Education Activity, establish controls necessary to discontinue the use of Operation and Maintenance funds for the acquisition of investment items with a cost in excess of the applicable investment item cost threshold, to make necessary accounting adjustments to deobligate Operation and Maintenance funds, and to obligate Procurement funds. In addition, the aggregate cost of the local area networks acquired with Operation and Maintenance funds exceeded the dollar thresholds Congress established for the use of Operation and Maintenance funds.

The Under Secretary of Defense (Comptroller) did not respond to the draft of the report. The Deputy Assistant Secretary of Defense (Personnel Support, Families, and Education) comments stated that an investigation would be initiated if the Under Secretary of Defense (Comptroller) so directs. The Department of Defense Education Activity generally concurred with the recommendations to discontinue the acquisition and installation of investment items with Operation and Maintenance funds and to obligate Procurement funds for the cost of investment items procured. However, the Department of Defense Education Activity disagreed that Antideficiency Act violations could have occurred, because it had Procurement funds to cover the accounting adjustments. In addition, the Department of Defense Education Activity disagreed with the report's definition of a "system," stating that the local area networks at the schools were individual stand-alone systems, based on the primacy of purpose of each system.

In response to Department of Defense Education Activity comments, the final report contains a joint recommendation to the Under Secretary of Defense (Comptroller) and the Deputy Assistant Secretary of Defense (Command, Control, Communications, and Intelligence) to provide guidance on the definition, acquisition, and appropriate funding for automated data processing equipment, including local area networks within DoD. Additional management comments were requested.

Inspector General, DoD, Report No. 97-073, "Reliability of the FY 1995 Financial Statements for the Defense Logistics Agency General Fund," January 15, 1997. The report states that for the Fund Balance with Treasury asset account, the DFAS Columbus Center did not fully comply with

Appendix C. Synopsis of FYs 1995 and 1996 Defense Agency Financial Statement Reports and Related Audit Reports

Department of the Treasury financial reporting guidance to disclose differences between summary disbursement and collection reports to the Treasury and the DLA general ledger accounts in supporting notes to the three FY 1995 DLA General Fund statements. In addition, the DFAS Columbus Center reported questionable balances in the Accounts Receivable asset account, Accounts Payable liability account, and the Revenue From Services Provided revenue account because those balances did not correspond to amounts in the DLA general ledger accounts. Consequently, the DLA General Fund financial information is of limited value and affects the reliability and usefulness of the consolidated DoD-wide financial statements for FY 1996. The report recommends that the DFAS Columbus Center fully disclose the reconciliation of the Fund Balance with Treasury account. In addition, the report recommends that the DLA use general ledger accounts instead of budget execution reports as data sources for financial statement account balances. The report also recommends that the DLA perform quality reviews of its financial statements to confirm the accuracy of the financial information therein. The DFAS Columbus Center concurred with all report recommendations and estimated that corrective actions will be completed by September 30, 1997.

Inspector General, DoD, Report No 97-065, "Funds Control at the Office of Civilian Health and Medical Program of the Uniformed Services," January 10, 1997. The report states that the OCHAMPUS financial accounting system did not accurately record reimbursable obligation authority. In addition, the OCHAMPUS reported a negative balance of \$1.07 billion in the Allotted Reimbursable Program at September 30, 1995, and a negative balance at the end of the 12 months in that fiscal year. Because the availability of funds was not accurately reflected in the financial records, the records were unreliable, and OCHAMPUS could have incorrectly approved obligations, resulting in a potential Antideficiency Act violation. The report recommends that OCHAMPUS investigate the potential Antideficiency Act violation, research the effect of incorrect recording of reimbursable obligation authority, and implement a change to the accounting system.

The report also states that the OCHAMPUS reported negative Funds with Treasury balances of \$193.9 million for FY 1994 and \$297.7 million for FY 1995. The negative balances occurred because OCHAMPUS disbursed funds for CHAMPUS health care costs before receiving reimbursement from the Military Departments and non-Defense agencies. Consequently, Antideficiency Act violations may have occurred. The report recommends that OCHAMPUS investigate the potential Antideficiency Act violations. The report also recommends that the Assistant Secretary of Defense (Health Affairs) establish policy for OCHAMPUS to receive direct citation of funds rather than seeking a reimbursement.

The Office of the Assistant Secretary of Defense (Health Affairs) concurred with recommendations to develop and implement procedures to accurately record the reimbursable obligation authority. The Assistant Secretary of Defense (Health Affairs) partially concurred with the recommendation to accept Military Interdepartmental Purchase Requests for direct citation of funds and proposed alternative actions. The Assistant Secretary partially concurred because of the potentially significant adverse ramifications its acceptance could

Appendix C. Synopsis of FYs 1995 and 1996 Defense Agency Financial Statement Reports and Related Audit Reports

have on disbursements and obligations. In addition, the Assistant Secretary nonconcurred with the recommendation to require advance payment from non-Defense agencies because to do so would violate Department of the Treasury regulations. Additional management comments were requested.

Inspector General, DoD, Report No. 97-059, "Financial Management for the Office of the Civilian Health and Medical Program of the Uniformed Services," December 27, 1996. The report states that the Office of the Civilian Health and Medical Program of the Uniformed Services (OCHAMPUS) did not properly process accounting transactions, comply with the Prompt Payment Act, establish and use subsidiary ledgers, make closing entries, and prepare financial reports and statements in accordance with financial regulations. Consequently, the FY 1994 monthly trial balances understated the accounts payable and expense accounts by an average of \$72.2 million per month, overstated the appropriated capital account by \$329,894, and overstated the automated data processing software and its related depreciation account by \$47,625.

The report also states that the FY 1995 OCHAMPUS monthly trial balances understated accounts payable and expense accounts by an average of \$67 million per month, overstated the appropriated capital account by \$329,894, and overstated the automated data processing software and related accounts by \$358,664. The report recommends that the OCHAMPUS clearly assign accounting responsibilities, separate accounting duties, supervise accounting staff, establish general ledger and financial statement training, and document accounting policies and procedures. The report also recommends that the Director, Acquisitions and Administration Directorate, OCHAMPUS, initiate additional accounting and control procedures, adjust accounting records, and establish and maintain subsidiary ledgers.

The Office of the Assistant Secretary of Defense (Health Affairs) responded for the Director, OCHAMPUS, and generally concurred with the recommendations. The Office of the Assistant Secretary stated that the planned actions would be complete by the second quarter, FY 1997. The Office of the Assistant Secretary nonconcurred with the recommendation to write off uncollectible recoupments because identifying uncollectible recoupments that had not reached the 10-year statutory limit would not be cost-effective. Additional management comments were requested.

Inspector General, DoD, Report No. 97-047, "Consolidated Financial Report on the National Guard and Reserve Equipment Appropriation for the Army National Guard," December 13, 1996. The report states that the Army National Guard FY 1995 general ledger included duplicate reporting of Military Equipment, misstated liabilities, and used a budgetary account incorrectly. In addition, the Army National Guard did not record accounts payable upon evidence of equipment receipt. As a result, the FY 1995 general ledger Military Equipment account was overstated by \$427.1 million, the Accounts Payable accounts were overstated by a total of \$5.1 million, and the Allotments Received account was misclassified as Anticipated Earned Authority-Defense Business Operations Fund.

Appendix C. Synopsis of FYs 1995 and 1996 Defense Agency Financial Statement Reports and Related Audit Reports

The report recommends that the Army National Guard make appropriate adjusting accounting entries and establish management controls for recording and reporting financial information for the National Guard and Reserve Equipment Appropriation. The Army National Guard stated that it had begun making the suggested accounting entries. The Army National Guard partially concurred with recommendations to establish management controls for recording and reporting financial information for the National Guard and Reserve Equipment Appropriation and stated that it lacked the visibility over receipt of equipment needed to record the liabilities. Additional comments were requested.

Inspector General, DoD, Report No. 97-045, "Financial Accounting at the Defense Intelligence Agency," December 12, 1996. The report states that DIA FY 1996 accounting records did not contain accurate financial information. The accounting records were inaccurate because the DIA did not include up to \$222.5 million in disbursements by others; did not comply with DoD capitalization thresholds; incorrectly recognized income and receivables prior to completion of reimbursable work orders; did not properly accrue liabilities and expenses; and did not verify the validity of travel advances. As a result, DIA financial information reported to the DFAS Indianapolis Center was not reliable. The report recommends that the DIA establish controls and standard operating procedures to correct several accounting system weaknesses.

The DIA generally concurred with the recommendations and stated that corrective actions have been or would be implemented. The DIA partially concurred with recommendations to record accrued liabilities from DIA field centers and to record employee payroll costs earned, but not paid. DIA based its conditional concurrence on programming changes the NSA plans to make in FY 1998 to the accounting system used by DIA. The DIA nonconcurred with the recommendation to record income and accounts receivable from reimbursements based on actual or constructive performance. DIA stated that it will request a waiver from the Office of the Secretary of Defense to continue to record earnings and accounts receivable from reimbursements based on obligations. Additional comments were requested on establishing procedures to record liabilities, which management indicated could be delayed until FY 1998.

Inspector General, DoD, Report No. 97-044, "Army National Guard Military Equipment," December 11, 1996. The report states that the Army National Guard FY 1995 general ledger military equipment account, Equipment in Use, included the cost of equipment with a unit cost that did not meet the DoD capitalization threshold. Also, the Army National Guard misstated the Military Equipment in Transit account as the Equipment in Use account. As a result, the Army National Guard FY 1995 general ledger account, Equipment in Use, was overstated by \$10.3 billion, and Equipment in Transit, was understated by \$1.2 billion. The report recommends that the Army National Guard record and report the value of military equipment using established capitalization thresholds, make adjusting entries, and document accounting procedures for recording and reporting military equipment transactions. The report also recommends that the Deputy Chief of Staff for Logistics provide general ledger account balances for military equipment to the Army National

Appendix C. Synopsis of FYs 1995 and 1996 Defense Agency Financial Statement Reports and Related Audit Reports

Guard for military equipment accounts. Further, the report recommends that the DFAS Indianapolis Center make appropriate accounting entries to accurately classify Army National Guard military equipment in the Army general ledger.

The National Guard Bureau, commenting for the Army National Guard, concurred with the recommendations and stated that it will complete corrective actions by March 1997. The DFAS Indianapolis Center stated that it cannot make correcting entries to Army National Guard reported data; however, the DFAS Indianapolis Center will advise the Army National Guard and request revisions if the data are not consistent with Army guidance.

Inspector General, DoD, Report No. 97-039, "Defense Logistics Agency General Fund Equipment Account," December 5, 1996. The report states that the DFAS Columbus Center erroneously included Defense Business Operations Fund equipment balances on the FY 1995 DLA General Fund trial balance. Consequently, the FY 1995 yearend balance of \$411 million of the DLA General Fund Equipment account was materially misstated. The report recommends that the DFAS Columbus Center adjust the DLA General Fund Equipment account balance to delete the Defense Business Operations Fund equipment accounts.

The report also states that the DFAS Columbus Center and DLA did not periodically compare the DLA General Fund Equipment account with custodial records. Consequently, the DLA General Fund Equipment account balance was not reliable, was not auditable, and may be overstated by at least \$85.2 million. The report did not recommend complete reconciliation of FY 1996 account balances because of cost for that effort and because of planned implementation of the Defense Property Accounting System. The report recommends that the DFAS Columbus Center provide equipment account balances to General Fund organizations as the Defense Property Accounting System is implemented.

The DLA and the DFAS concurred with the recommendations in the report. The DLA concurred with the recommendation to annually reconcile its custodial records with the proprietary equipment account balance in the Defense Property System. The DLA also agreed to report the management control weakness in its Annual Statement of Assurance. The DFAS concurred with the recommendations and stated that corrective actions were completed before September 30, 1996. Additional comments were requested to obtain information on actions taken by management.

Inspector General, DoD, Report No. 97-025, "Consolidated Financial Report on the National Guard and Reserve Equipment Appropriation for the Army Reserve," November 19, 1996. The report states that the DFAS Indianapolis Center omitted expense information in preparing the FY 1995 Army Reserve trial balance for the National Guard and Reserve Equipment Appropriation. As a result, expenses on the FY 1995 trial balance were understated, and on the FY 1996 financial statements, equity will be overstated by \$70.1 million. The report recommends that the DFAS Indianapolis Center improve its procedures for extracting Army Reserve financial information. In addition, the report recommends that the DFAS Indianapolis Center establish management controls to verify the completeness of financial information used to

Appendix C. Synopsis of FYs 1995 and 1996 Defense Agency Financial Statement Reports and Related Audit Reports

prepare financial statements and adjust the FY 1996 Army Reserve trial balance accordingly. Also, the report recommends that the DFAS Indianapolis Center adjust the Appropriated Capital account balance by \$70.1 million for the FY 1996 National Guard and Reserve Equipment Appropriation.

The DFAS Indianapolis Center agreed to improve its procedures to include all relevant financial information in financial statements. In addition, the DFAS Indianapolis Center agreed to establish management controls to ensure the completeness of the information extracted for the financial statements. Also, the DFAS Indianapolis Center partially concurred with the recommendation to adjust the Appropriated Capital account balance because corrective actions taken would eliminate the need to adjust the Appropriated Capital account balance.

Inspector General, DoD, Report No. 97-024, "General Fund Trial Balance of the Defense Logistics Agency at September 30, 1995," November 15, 1996. The report states that the DFAS Columbus Center had not identified and corrected imbalances totaling \$543 million between the general and supporting subsidiary ledgers and imbalances totaling \$894 million between equivalent proprietary and budgetary general ledger accounts. In addition, the DFAS Columbus Center accounting system did not provide an audit trail to identify and correct the imbalances. Consequently, the DLA trial balance was unreliable and unauditible, and there was no assurance that the resultant DLA financial statements were accurate. The report recommends that the DFAS Columbus Center accelerate implementation of accounting system changes needed to readily identify and correct account imbalances, provide the needed audit trail to correct identified imbalances, and reconcile accounts so that the DLA FY 1996 financial statements can be more reliable. The DFAS Columbus Center stated that it is committed to identifying and correcting the cause of the imbalance and is trying to resolve it. Additional comments were requested to clarify how management actions taken will help identify and correct account imbalances.

Inspector General, DoD, Report No. 97-020, "Capitalization of Defense Technology Security Administration Equipment," November 4, 1996. The report states that the Defense Technology Security Administration (DTSA) FY 1995 general ledger military equipment account, Equipment in Use, included the cost of equipment and software with a unit cost that did not meet the DoD capitalization threshold and contract services that were not part of the acquisition costs of equipment. As a result, DTSA overstated general ledger asset accounts and general ledger equity accounts by \$1.6 million in FY 1995.

The report recommends that Washington Headquarters Services (WHS) reestablish controls in the WHS Allotment Accounting System and revise operating procedures to correctly report the amount of DTSA capitalized equipment. In addition, the report recommends that the Director, DFAS Indianapolis Center, make adjusting entries to exclude the cost of noncapital acquisitions from the WHS Allotment Accounting System; to establish operating procedures for information required from Defense agencies to properly record the status of equipment disposals and to establish accounting controls to ensure that the Equipment in Use account accurately reflects the acquisition cost of equipment placed in use. The WHS agreed with the recommendations and has

Appendix C. Synopsis of FYs 1995 and 1996 Defense Agency Financial Statement Reports and Related Audit Reports

initiated corrective actions. The DFAS Indianapolis Center proposed responsive alternative actions regarding the recommendations.

Inspector General, DoD, Report No. 97-017, "Consolidated FY 1995 Financial Report on Defense Organizations Receiving Department 97 Appropriations," October 31, 1996. The report states that 29 Defense organizations reported adjusted trial balances to the DFAS Indianapolis Center. However, 19 of the 29 Defense organizations used data from sources other than a general ledger accounting system to prepare their FY 1995 adjusted trial balances. Also, the DFAS Indianapolis Center had not established the management controls necessary to ensure that all FY 1995 Department 97 fund recipients provided complete financial information for the preparation of the DoD consolidated Department 97 financial report. As a result, about \$19 billion of Department 97 funding was not controlled through a general ledger accounting control system and about \$820 million of FY 1995 funding was omitted from the Defense organizations' FY 1995 adjusted trial balance submissions to the DFAS Indianapolis Center. Further, more than 50 percent of the FY 1996 Department 97 appropriation will not be controlled by complete general ledger accounting control systems. The report recommends that the DFAS Indianapolis Center establish procedures and management controls to ensure that all Department 97 fund recipients provide financial reports in compliance with Federal guidance. The DFAS concurred with the finding and recommendations and stated that corrective actions would be completed during FY 1997.

Inspector General, DoD, Report No. 96-215, "Financial Management at the Defense Advanced Research Projects Agency," August 28, 1996. The report states that Navy and Air Force accounting organizations responsible for accounting for the suballocations of FY 1995 funds from the Defense Advanced Research Projects Agency (DARPA) did not provide complete and accurate adjusted trial balance information to the DFAS Indianapolis Center. As a result, the FY 1995 DARPA adjusted trial balance was understated by at least \$697 million. In addition, the FY 1995 military equipment trial balance was understated by \$48 million.

The report recommends that DARPA research organizations prepare the adjusted trial balances needed to generate Department 97 financial reports. The report also recommends that DARPA request that DoD research organizations report the value of research equipment purchased with Research, Development, Test, and Evaluation suballocations from DARPA and that DoD research organizations review DARPA equipment accounts to make adjusting entries to eliminate capitalized equipment that does not meet the DoD capitalization threshold. The Navy and DFAS Indianapolis Center generally concurred with the recommendations and stated that corrective actions were taken. The DARPA concurred with the recommendation to inform DoD research organizations of their responsibility to report the value of research equipment that meets DoD capitalization thresholds.

Inspector General, DoD, Report No. 96-213, "Financial Accounting at the National Security Agency," August 20, 1996. The financial accounting system NSA used was capable, if modified, of producing information necessary

Appendix C. Synopsis of FYs 1995 and 1996 Defense Agency Financial Statement Reports and Related Audit Reports

for financial statements required by the Chief Financial Officers Act. However, correcting deficiencies in the accounting system and establishing effective management controls are essential to produce accurate financial statements to be included in the DoD consolidated statements.

The NSA had not programmed the accounting system to produce necessary information for developing financial statements, balances in supporting records were not reconciled to control accounts in the general ledger, expenses and liabilities were not recorded until disbursements were made, and procedures were not established to calculate and record accrued payroll liabilities. Also, recorded balances of equipment, real property, and inventory were incorrect, misstated, or not supported. As a result, the general ledger and supporting information could not be relied on for information necessary to produce accurate financial statements required by the Chief Financial Officers Act.

The report recommends that the NSA follow DoD capitalization criteria, reconcile general ledger control accounts with supporting documentation, and establish procedures and management controls to ensure that the general ledger contains reliable financial information. The NSA concurred with the audit report recommendations and agreed to take recommended actions.

Inspector General, DoD, Report No. 96-212, "Capitalization of DoD General Property, Plant, and Equipment," August 19, 1996. The report states that, in accounting for assets, the DoD Components capitalized and retained in the financial records low-cost items that were below the current capitalization threshold. Therefore, the \$9.6 billion value of equipment reported in the Military Equipment account for FY 1995 is of limited utility for financial management purpose. The report recommends that the Chief Financial Officer direct the DoD Components to apply one capitalization threshold to general property, plant, and equipment accounts and to adjust financial records accordingly. The Chief Financial Officer generally concurred with the report recommendation and is taking action to change the DoD capitalization threshold.

Appendix D. Management Control Programs

DoD Directive 5010.38, "Management Control (MC) 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.

Management control weaknesses, as defined by DoD Directive 5010.38, existed at the DFAS Indianapolis and Columbus Centers, DTSA, DIA, Army National Guard, NSA, DARPA, OCHAMPUS, DLA, Department of Defense Education Activity, and the Army Reserves. The weaknesses at each agency are discussed below.

Adequacy of Management Controls at the DFAS Centers

Seven audit reports identified material management control weaknesses at the DFAS Indianapolis and Columbus Centers. The weaknesses were identified during audits of Defense agencies' financial information (see Appendix C).

Documentation of the Federal Financial System Process at the DFAS Indianapolis Center (Discussed in Inspector General, DoD, Report No. 97-079, January 24, 1997). The DFAS Indianapolis Center prepares financial statements for Defense agencies, including the Army Reserves' portion of the National Guard and Reserve Equipment Appropriation. The DFAS Indianapolis Center did not document the process for receiving, adjusting, and consolidating the monthly general ledger trial balance submitted by the Army Reserves' fiscal stations. The lack of documentation is a material management control weakness and a material departure from KAR 10. The DFAS Indianapolis Center did not review its compliance with KAR 10, because it did not identify the process of documenting the system as an assessable unit and, therefore, did not identify the material management control weakness.

DFAS Indianapolis Center Support for the Army Reserves (Discussed in Inspector General, DoD, Report No. 97-025, November 19, 1996). A material management control weakness was attributed to the DFAS Indianapolis Center because it did not have sufficient controls in place, such as completeness checks, to ensure that all data necessary for the general ledger trial balances for the Army Reserve were extracted. The DFAS Indianapolis Center Annual Statement of Assurance did not report the insufficient procedures for extracting financial information from data bases as a material weakness. As a result, expenses on the FY 1995 trial balance are understated, and on the FY 1996 financial statements, equity will be overstated by \$70.1 million.

DFAS Indianapolis Center Support for DTSA (Discussed in Inspector General, DoD, Report No. 97-020, November 4, 1996). A material management control weakness was attributed to the DFAS Indianapolis Center because it did not have standard operating procedures in place to ensure that disposed of assets were removed from the appropriate accounts. Also, DFAS Indianapolis Center management controls for reporting Equipment in Use transactions were not adequate to ensure that the transactions were properly capitalized or expensed. The DFAS Indianapolis Center Annual Statement of Assurance did not report the lack of procedures for the reporting of disposed assets by supported organizations as a material weakness.

DFAS Indianapolis Center Consolidation of Department 97 Appropriations (Discussed in Inspector General, DoD, Report No. 97-017, October 31, 1996). The DFAS Indianapolis Center management controls for the consolidation of the Department 97 adjusted trial balances were not sufficient to ensure that financial reports the DFAS Indianapolis Center prepares are supportable, reliable, and accurate. In addition, the DFAS Indianapolis Center did not establish documented operating procedures to ensure that the process for preparing financial reports is consistent, timely, and auditable. The DFAS Indianapolis Center did not assess the consolidation of the Department 97 adjusted trial balances as part of the DFAS Indianapolis Center management control program and, therefore, did not detect and report the management control weaknesses.

Reliability of Defense Logistics Agency Financial Statements (Discussed in Inspector General, DoD, Report No. 97-073, January 15, 1997). The DFAS Columbus Center prepared the FY 1995 financial statements for the eight DLA General Fund appropriations. The audit reviewed the FY 1995 trial balances for three of the eight appropriations and found material management control weaknesses at the DFAS Columbus Center. The DFAS Columbus Center managers did not comply with Department of the Treasury financial reporting guidance, which requires organizations to disclose material differences in notes to the financial statements. The DLA did not report material differences between summary disbursement and collection reports and the DLA general ledger accounts. In addition, the DFAS Columbus Center did not comply with DoD financial reporting guidance and improperly approved the use of budget execution reports instead of general ledger accounts as data sources for the three DLA General Fund statements. Finally, the DFAS Columbus Center managers did not establish and require quality control reviews of the DLA General Fund statements after preparation to confirm the accuracy of the statements.

The DFAS Columbus Center managers did not identify as an assessable unit the financial statements that DoD organizations are required to prepare for submission to the Treasury. However, the managers did identify as an assessable unit the financial statements that DoD organizations are required to prepare for submission to the Office of Management and Budget under Public Law 101-576 and, in our opinion, correctly identified the risk associated with the assessable unit as high. The DFAS Columbus Center managers' evaluations did not identify the same management control weaknesses identified by the audit because the evaluation covered only the financial statements for Defense

Appendix D. Management Control Programs

Business Operations Fund organizations. The DFAS Columbus Center management initiated responsive actions that will be completed by September 30, 1997.

Adequacy of Controls Over the Defense Logistics Agency General Fund Equipment Account (Discussed in Inspector General, DoD, Report No. 97-039, December 5, 1996). Management controls at the DFAS Columbus Center were not effective to provide reasonable assurance that material misstatements in the DLA General Fund Equipment account would be prevented or detected in a timely manner. The management controls over the DLA General Fund Equipment account were materially deficient because the DFAS Columbus Center accounting system did not permit the identification and location of general fund equipment as reported on the FY 1995 general fund trial balance.

The DFAS Columbus Center identified financial accounting of capital equipment as part of an assessable unit and, in our opinion, correctly identified the risk associated with financial accounting of capital equipment as high. However, the DFAS Columbus Center evaluation did not identify the specific material management control weaknesses identified by the audit because coverage at the center was broad.

The DFAS Columbus Center reported two departures to General Accounting Office accounting principles, standards, and related requirements in its FY 1994 Annual Statement of Assurance. The DFAS Columbus Center reported that the Base Operating Support System, a subsystem to the Defense Business Management System, did not properly account for capital assets, and non-Defense Business Operations Fund proprietary accounts were not maintained at an organizational level in the Defense Business Management System.

Reliability of Defense Logistics Agency Trial Balance (Discussed in Inspector General, DoD, Report No. 97-024, November 15, 1996). The DFAS Columbus Center prepared the FY 1995 trial balance for the DLA using the Defense Business Management System. The audit reviewed the DFAS process for developing a trial balance for FY 1995 DLA general funds. The DFAS Columbus Center had material weaknesses for identifying and reconciling imbalances between control and subsidiary accounts. DFAS Columbus Center officials identified the weaknesses, but had not implemented accounting system changes for DLA General Fund appropriations.

Headquarters, DFAS, identified the reconciliation of the general ledger to supporting subsidiary ledgers and the existence of audit trails from financial statements to source documents as assessable units within the Defense Business Management System. Headquarters, DFAS, personnel conducted an evaluation for FY 1995, but did not identify the material weaknesses identified by the audit because their evaluation emphasized the Defense Business Management System's capabilities to perform the accounting functions for the Defense Business Operations Fund. DFAS also did not identify the need to reconcile proprietary with budgetary general ledger accounts as an assessable unit. However, the DFAS Columbus Center was drafting an instruction, specifying the need to reconcile proprietary and budgetary general ledger accounts.

Adequacy of Management Controls at Defense Agencies

Ten audit reports identified material management control weaknesses at eight Defense agencies. The weaknesses were identified during audits of the Defense agencies' financial information (see Appendix C).

Adequacy of Controls for Property Accountability at the Department of Defense Education Activity (Discussed in Inspector General, DoD, Report No. 97-082, January 28, 1997). The DoD Education Activity manages and supervises DoD Dependents Schools and uses the Dependents Schools Automated Material Management System to account for and control property. The report states that management control weaknesses over property accountability existed in the DoD Dependents Schools-Europe region. In the Annual Statement of Assurance, the Department of Defense Education Activity included property accountability as an area requiring management's attention and initiated actions to improve the accuracy of accountable property reporting. The management control program for the Department of Defense Education Activity was evaluated in Inspector General, DoD, Report No. 96-181, "Management Control Environment for the Department of Defense Education Activity," June 28, 1996. The audit showed that the Department of Defense Education Activity management control program was not adequately implemented. The report states that the Department of Defense Education Activity did not have an adequate control environment, did not have a general ledger accounting system, and did not adequately implement its management control program and review accounting system controls, as required. After issuance of the report, the Department of Defense Education Activity initiated actions to establish an independent internal review organization, modify yearend spending procedures, improve accounting guidance, improve the reliability of accounting reports, and use a general ledger system.

Office of the Civilian Health and Medical Program of the Uniformed Services. Two audit reports identified material management control weaknesses at OCHAMPUS.

Inspector General, DoD, Report No. 97-059, December 27, 1996. The OCHAMPUS had material management control weaknesses in that controls over financial management, accounting, and accounting systems were not adequate to ensure that OCHAMPUS records supported financial decisions, that OCHAMPUS accounted for transactions properly and reported results reliably, and that OCHAMPUS systems recorded transactions consistently with DoD general ledger requirements.

The OCHAMPUS identified financial management, accounting and accounting systems as assessable units and evaluated the risks as low to medium. In addition, in its FY 1995 self-evaluation, OCHAMPUS management identified departures from accrual accounting and from recording accounts payable; however, OCHAMPUS management did not consider the departures material and initiated system change requests to correct the departures. The OCHAMPUS did not identify all weaknesses identified in Report No. 97-059 because OCHAMPUS did not compare account balances with DoD guidance to

Appendix D. Management Control Programs

identify irregular balances or to compare balances from year to year to identify significant changes. OCHAMPUS management initiated responsive actions that will be completed by the end of the second quarter, FY 1997.

Inspector General, DoD, Report No. 97-065, January 10, 1997. The audit identified material management control weaknesses in that OCHAMPUS controls over the financial systems, disbursements, Federal Government billing, and reimbursements were not adequate to ensure that the OCHAMPUS financial system recorded transactions consistently with DoD general ledger requirements and that OCHAMPUS complied with Antideficiency Act requirements.

The OCHAMPUS FY 1995 self-evaluations identified the financial systems, disbursements, and Government billing as assessable units and evaluated the risks as low to medium. In addition, the OCHAMPUS self-evaluation identified departures from accrual accounting and from recording accounts payable; however, OCHAMPUS management did not consider the departures material and initiated system change requests to correct the departures. OCHAMPUS management did not identify all the weaknesses included in Report No. 97-065 because management did not compare account balances to DoD guidance to identify negative balances. OCHAMPUS management initiated responsive actions that will be completed by the end of the second quarter, FY 1997.

Adequacy of Management Controls at the Defense Intelligence Agency (Discussed in Inspector General, DoD, Report No. 97-045, December 12, 1996). The DIA management control program had weaknesses because the DIA had not established controls to ensure that disbursements by others were correctly accounted for, promptly recorded, and reported. Also, accountability, control, and reporting of equipment were not sufficient to provide reasonable assurance that primary control objectives were met. In addition, controls over posting and billing reimbursable customers and in verifying the validity of advances and liabilities needed improvement. The DIA did not identify the material management control weaknesses in its Annual Statement of Assurance because DIA self-evaluations did not use control checklists tailored for each assessable unit's objectives.

Army National Guard. Two audit reports identified material management control weaknesses at the Army National Guard.

Inspector General, DoD Report No. 97-047, December 13, 1996. The Army National Guard did not properly record and report transactions in the general ledger and did not maintain subsidiary ledgers to support general ledger account balances. The Army National Guard did not review its compliance with KAR 1, General Ledger Control and Financial Reporting and, therefore, did not identify the material management control weaknesses.

Inspector General, DoD Report No. 97-044, December 11, 1996. The Army National Guard did not have management controls to ensure that only military equipment assets that met the Army capitalization threshold were capitalized. The Guard also did not have management control techniques to ensure that military equipment assets included in the general ledger were

properly classified. The Army National Guard did not identify the material management control weaknesses in its Annual Statement of Assurance because the Guard did not assess the risk of recording in the general ledger, the military equipment assets that did not meet the Army capitalization threshold and did not assess the risk of not properly classifying recorded assets.

Adequacy of Controls Over the Defense Logistics Agency General Fund Equipment Account (Discussed in Inspector General, DoD, Report No. 97-039, December 5, 1996). Management controls at the DLA were not effective to provide reasonable assurance that material misstatements in the DLA General Fund Equipment account would be prevented or detected in a timely manner. The controls were not adequate because DLA did not perform periodic comparisons of the DLA General Fund Equipment account with custodial records.

The DLA identified financial accounting of capital equipment as part of an assessable unit and, in our opinion, correctly identified the risk associated with financial accounting of capital equipment as high. However, the DLA evaluation did not identify the specific material management control weaknesses identified by the audit because the DLA coverage was broad. The DLA reported inaccurate reporting of property, plant, and equipment on the FYs 1994 and 1995 financial statements as a material weakness and reported a target completion date for implementation of the Defense Property Accounting System as FY 1996. Although the Annual Statements of Assurance reported only the weaknesses for the Defense Business Operations Fund, corrective action was also under way at the General Fund organizations:

Adequacy of Management Controls at the Defense Technology Security Administration (Discussed in Inspector General, DoD, Report No. 97-020, November 4, 1996). The DTSA management controls were not adequate to ensure that assets no longer used were removed from the appropriate accounts. The DTSA acknowledged that inadequate property accountability is a condition that has not been corrected, but has not reported property accountability as a material weakness in its Annual Statement of Assurance. As a result of our audit, DTSA changed receiving procedures to link receiving reports to purchase documents and revised its procedures for excess and turn-in equipment.

Adequacy of Controls at the Defense Advanced Research Projects Agency (Discussed in Inspector General, DoD, Report No. 96-215, August 28, 1996). The DARPA management controls for financial asset accountability were not sufficient to assure correct financial statement reporting for research equipment used on DARPA funded projects. DARPA did not identify the material management control weakness because DARPA had not addressed the requirement of accounting for research equipment with the organizations to which it suballocates funds or the need to report those assets on the monthly and yearend DARPA trial balance.

Appendix D. Management Control Programs

Adequacy of Controls at the National Security Agency (Discussed in Inspector General, DoD, Report No. 96-213, August 20, 1996). The NSA had management control weaknesses in that accountability, control, and reporting of real and personal property was not sufficient to provide reasonable assurance that primary control objectives were met. Also, NSA had not established controls to ensure that required reports to DFAS and account balances in the consolidated general ledger were supported in subsidiary ledgers.

The NSA correctly reported the "accountability, control, and reporting of Agency fixed assets and other personal property . . ." as a material weakness in its Annual Statement of Assurance since 1988. However, the target dates for required corrective actions have been continually pushed back. Also, the Annual Statement of Assurance included corrective actions to correct only personal property accountability and reporting and not real property accountability and reporting.

Appendix E. Defense Agencies Audited

American Forces Information Service
Army National Guard
Army Reserves
Ballistic Missile Defense Organization
Central Imagery Office (now the National Imagery and Mapping Agency)
Corporate Information Management
Defense Acquisition University
Defense Advanced Research Projects Agency
Defense Contract Audit Agency
Defense Information Systems Agency
Defense Intelligence Agency
Defense Investigative Service
Defense Legal Services Agency
Defense Logistics Agency
Defense Mapping Agency (now the National Imagery and Mapping Agency)
Defense Medical Program Activity
Defense Prisoner of War/Missing in Action Office
Defense Special Weapons Agency
Defense Technology Security Administration
Department of Defense Education Activity
Federal Energy Management Program
Inspector General
Joint Staff
National Security Agency
Office of Civilian Health and Medical Program of the Uniformed Services
Office of Economic Adjustment
Office of the Secretary of Defense
On-Site Inspection Agency
Special Operations Command
Uniformed Services University of the Health Sciences
Washington Headquarters Services

Appendix F. Synopses of FY 1994 Financial Statement Reports and Related Audit Reports

Inspector General, DoD, Report No. 96-194, "The Capitalization of Washington Headquarters Services Military Equipment, July 16, 1996. The report states that the Washington Headquarters Services (WHS) FY 1994 general ledger military equipment account, Equipment in Use, included the cost of office furniture, furnishings, and fixtures with unit costs that did not meet DoD capitalization criteria; contract services were inappropriately classified as acquisition costs of equipment; and unit costs for computer equipment did not meet DoD capitalization criteria. As a result, WHS overstated general ledger asset accounts and general ledger equity accounts by at least \$16.3 million in FY 1994. The WHS initiated actions during the audit to remove from the Equipment in Use account \$9.5 million that reflected office furniture, furnishings, and fixtures transactions with unit costs that did not meet capitalization criteria. WHS also corrected a flaw in the WHS Allotment Accounting System that inappropriately recorded equipment procured for other DoD organizations in the WHS military equipment account. The report recommends that WHS reduce the amount of its Equipment in Use account and its general ledger Equity account by \$6.8 million. The report also recommends that the WHS establish accounting controls to ensure that military equipment transactions are correctly capitalized and that WHS review past transactions and expense those costs that do not meet DoD capitalization criteria. The WHS had taken responsive corrective actions.

Inspector General, DoD, Report No. 96-155, "The Defense Information Systems Agency General Ledger Military Equipment Account," June 10, 1996. The report states that the Defense Information Systems Agency (DISA) general ledger asset account, Equipment in Use, was significantly overstated. The Equipment in Use account inappropriately included the acquisition cost of military equipment transferred to other DoD Components; military equipment loaned or furnished to other DoD Components, Federal Agencies, and DoD contractors; computer software that should have been recorded in another asset account; and military equipment and other services that should have been expensed. The overstatements occurred because DISA did not analyze financial transactions needed to make appropriate accounting entries. In addition, DISA did not record in its official property records the military equipment loaned or furnished to other DoD Components, Federal Agencies, and DoD contractors. As a result, DISA overstated military equipment in use by about \$93.7 million and misstated general ledger accounts. The report recommends that DISA analyze military equipment transactions and make appropriate accounting entries to accurately record military equipment transactions in the DISA general ledger; record in the official DISA property book military equipment loaned and furnished to other DoD Components, Federal Agencies, and contractors; and establish appropriate control techniques to ensure that military equipment transactions are accurately recorded in the general ledger and DISA property records. The DISA concurred with all recommendations and has initiated corrective actions.

Appendix F. Synopses of FY 1994 Financial Statement Reports and Related Audit Reports

Inspector General, DoD, Report No. 96-088, "Inventory at the Defense Mapping Agency," March 26, 1996. The report states that the physical count of Defense Mapping Agency (DMA) (now the National Imagery and Mapping Agency) inventory differed from the quantities in accountable records, unit costs of DMA products were incorrect and lacked supporting documentation, and inventory on hand exceeded inventory usage history. As a result, about 83 percent of reported inventory balances at DMA Philadelphia was incorrect, accounting records could not be relied on to produce accurate financial statements, and DMA records showed that about 30 percent of the recorded inventory was excess to inventory stock level objectives. The report recommends that DMA perform a wall-to-wall inventory of its products and make appropriate adjustments to accountable records. The report also recommends that the DMA value and report inventory based on historical costs, establish controls to assure that unit costs are supported and accurate, and identify excess inventory in financial reports. The DMA concurred with the recommendations and stated that controls and procedures either had been or would be established to correct each problem.

Inspector General, DoD, Report No. 96-083, "Accounting Support for Preparation of Joint Chiefs of Staff Financial Statements," March 12, 1996. The report states that the FY 1994 Joint Staff financial statements, prepared by the DFAS DAO/WHS, were inaccurate. The DFAS Defense Accounting Office/Washington Headquarters Services (DFAS DAO/WHS) reported Joint Staff Research, Development, Test, and Evaluation funds to the DFAS Indianapolis Center on two separate financial statements, resulting in an overstatement of Joint Staff assets of about \$48 million. In addition, to determine the equity for the FY 1994 Joint Staff financial statements, the DFAS DAO/WHS calculated equity amounts using information from budget execution reports instead of using proprietary general ledger account information. The budget execution reports did not contain the information needed to prepare complete and accurate FY 1994 financial statements. No recommendations were made because recommendations in prior audit reports should remedy the identified deficiencies.

Inspector General, DoD, Report No. 96-068, "Accounting Support for Preparation of Ballistic Missile Defense Organization Financial Statements," February 9, 1996. The report states that the FY 1994 financial statements prepared by the DFAS DAO/WHS were inaccurate and incomplete. The DFAS DAO/WHS reported Ballistic Missile Defense Organization Research, Development, Test, and Evaluation funds to the DFAS Indianapolis Center on two separate financial statements, resulting in overstatements of Ballistic Missile Defense Organization asset, liability, and equity accounts. In addition, the DFAS DAO/WHS used budgetary information from budget execution reports instead of using proprietary general ledger account information to prepare Ballistic Missile Defense Organization FY 1994 financial statements. Budget execution reports did not contain needed information to prepare complete and reliable FY 1994 financial statements. The report identified errors and omissions, totaling about \$1.9 billion, in 12 financial statement accounts. No recommendations were made because recommendations in prior audit reports should remedy the noted deficiencies.

Appendix F. Synopses of FY 1994 Financial Statement Reports and Related Audit Reports

Inspector General, DoD, Report No. 96-048, "Defense Accounting Office, Washington Headquarters Services, Procedures for Preparing FY 1994 Financial Statements for the Advanced Research Projects Agency," December 19, 1995. The report states that the DFAS DAO/WHS had not implemented DoD financial management directives and related guidance for preparing Advanced Research Projects Agency (now the Defense Advanced Research Projects Agency) financial statements. The DFAS DAO/WHS prepared consolidated financial statements for the Advanced Research Projects Agency using budget execution reports instead of proprietary trial balances. Consequently, the DFAS DAO/WHS prepared financial statements that overstated the Advanced Research Projects Agency financial position by \$2.2 billion in assets, \$25 million in liabilities, and \$2.2 billion in equity. The report recommends that the DFAS DAO/WHS establish procedures to verify that Advanced Research Projects Agency financial statements for FY 1996 and subsequent years are prepared in accordance with DoD 7000.14-R, "Financial Management Regulation," volume 1, May 1993, and DoD Directive 7220.9-M, "DoD Accounting Manual, chapter 94, October 1983. In addition, the report recommends that DFAS train employees assigned to prepare general-purpose financial statements in how to prepare the statements properly and accurately. DFAS concurred in general with the recommendations and took corrective actions.

Inspector General, DoD, Report No. 96-042, "Corporate Information Management Financial Statements," December 11, 1995. The report states that the FY 1994 Corporate Information Management trial balance, prepared by the WHS, omitted Corporate Information Management funds that the Office of the Assistant Secretary of Defense (Command, Control, Communications, and Intelligence) suballocated to DISA and to the Military Departments. However, the Office of the Assistant Secretary of Defense implemented management control procedures during the audit to assist in producing a complete Corporate Information Management trial balance and auditable Corporate Information Management financial statements. The report contains no findings or recommendations.

Inspector General, DoD, Report No. 96-039, Financial Accounting for the Defense Nuclear Agency," December 11, 1995. The report states that the financial accounting system used by the Defense Nuclear Agency (now the Defense Special Weapons Agency) was in substantial compliance with DoD accounting requirements. However, correction of certain deficiencies was essential to produce accurate and auditable financial statements needed to support DoD consolidated statements. The general ledger module contained computer programming errors and omissions; necessary subsidiary records and general ledger accounts had not been established; some recorded account balances were incorrect or insupportable; and general ledger transaction histories were erased at the end of each fiscal year. As a result, the general ledger and supporting information could not be relied on for information necessary to produce auditable and reliable financial statements required by the Chief Financial Officers Act. The report recommends that the Defense Nuclear Agency correct computer logic errors in its financial accounting system, adjust general ledger accounts for incorrect balances, establish necessary subsidiary

Appendix F. Synopses of FY 1994 Financial Statement Reports and Related Audit Reports

ledgers, and retain general ledger transaction histories. The Defense Nuclear Agency concurred with the recommendations and stated that corrective actions would be completed by December 31, 1996.

Inspector General, DoD, Report No. 96-003, "Defense Information Systems Agency FY 1994 General-Purpose Financial Statements," October 5, 1995. The report states that DISA did not use the DoD approved standard general ledger account structure to prepare FY 1994 general-purpose financial statements. Instead, DISA used the budget execution reports as the data source for the financial statements, because DISA personnel had not been trained in the relationship between the general ledger account structure and financial statements and because the DISA management control program was not adequate to ensure that financial statements were prepared using proper sources of information. As a result, DISA FY 1994 financial statements were materially inaccurate and incomplete. The report recommends that DISA use the DoD approved general ledger account structure to prepare future financial statements, train employees assigned to prepare financial statements, and implement adequate management control procedures. The DISA concurred with all recommendations and implemented corrective actions.

DISA did not request and the WHS did not make annual general ledger account closing entries to close accounts in the DISA general ledger account structure. The closing entries were not made because WHS and DISA did not clearly define responsibilities for making annual closing entries. As a result, the DISA FY 1995 opening general ledger account structure included materially incorrect balances. The report recommends that the WHS and DISA clarify responsibilities for making general ledger accounting closing entries. The WHS and DISA concurred with the recommendations and took corrective actions.

Inspector General, DoD, Report No. 95-231, "Vendor Payments-Defense Accounting Office, Air Force District of Washington, Finance Washington," June 12, 1995. The report states that the DFAS DAO/WHS made incorrect or improper payments, improperly certified vouchers, did not update the accounting system, and did not maintain proper supporting documentation. Further, the DFAS DAO/WHS did not adequately use exception reports that identified accounting errors to ensure the integrity of accounting information, did not consistently perform certification of fund availability, and had not implemented a management control program. The report recommends that the Director, DFAS, make improvements in accounting procedures, recoup duplicate payments, maintain adequate source documentation, certify fund availability, and implement a management control program. The Deputy Director for Finance, DFAS, agreed with all recommendations except for requiring that the disbursing officer certify fund availability. Corrective actions taken include validating and recouping duplicate payments; correcting erroneous payments; establishing procedures to minimize duplicate and erroneous payments; and establishing an accounting system training program, uniform filing procedures, and a management control program.

Appendix G. Accounting System Weaknesses at the Defense Agencies

KAR	1	2	3	5	7	8	9	10	11	12
Agency										
AFIS	W/D	--	--	--	--	--	--	W/D	--	--
ARMYRES	W	--	--	--	--	--	--	W/D	--	--
ARNG	W	W	--	--	W	--	W	W/D	--	--
BMDO	W/D	--	--	--	--	--	--	W/D	--	--
CIM	--	--	--	--	--	--	--	W/D	--	--
CIO	--	--	--	--	--	--	--	W/D	--	--
DARPA	W/D	W	--	--	W	--	--	W/D	--	--
DAU	W/D	--	--	--	--	--	--	W/D	--	--
DCAA	W/D	--	--	--	--	--	--	W/D	--	--
DIA	--	W	W	W	--	--	W	W/D	--	--
DISA	W/D	--	--	--	--	--	--	W/D	--	--
DIS	W/D	--	--	--	--	--	--	W/D	--	--
DLA	W/D	W	--	--	W/D	W/D	--	W/D	--	--
DLSA	--	--	--	--	--	--	--	W/D	--	--
DMA	W/D	--	--	--	--	--	--	W/D	--	--
DMPA	W/D	--	--	--	--	--	--	W/D	--	--
DSWA	--	--	--	--	--	--	--	W/D	--	--
DTSA	--	W	--	--	--	--	--	W/D	--	--
DoDEA	W/D	W	--	--	W	--	--	W/D	--	--
FEMP	W/D	--	--	--	--	--	--	W/D	--	--
IG	--	--	--	--	--	--	--	W/D	--	--
JS	W/D	--	--	--	--	--	--	W/D	--	--
NSA	W	W	W	W	--	--	--	W/D	--	--
OCHAMPUS	W/D	W	W	W	W	--	W	W/D	W	W
OEA	W/D	--	--	--	--	--	--	W/D	--	--
OSD	W/D	W	--	--	--	--	--	W/D	--	--
OSIA	--	--	--	--	--	--	--	W/D	--	--
POW/MIA	--	--	--	--	--	--	--	W/D	--	--
SOC	W/D	--	--	--	--	--	--	W/D	--	--
USUHS	W/D	--	--	--	--	--	--	W/D	--	--
WHS	W/D	--	--	--	--	--	--	W/D	--	--

W Weakness at agency
W/D Weakness at DFAS (supporting accounting office)
-- No Weakness noted

See Defense agencies listed on the following page.

Appendix G. Accounting System Weaknesses at the Defense Agencies

Acronyms

AFIS	American Forces Information Service
ARMYRES	Army Reserves
ARNG	Army National Guard
BMDO	Ballistic Missile Defense Organization
CIM	Corporate Information Management
CIO	Central Imagery Office
DAU	Defense Acquisition University
DCAA	Defense Contract Audit Agency
DIS	Defense Investigative Service
DMPA	Defense Medical Program Activity
DoDEA	Department of Defense Education Activity
DSWA	Defense Special Weapons Agency
FEMP	Federal Energy Management Program
OEA	Office of Economic Adjustment
OSD	Office of the Secretary of Defense
OSIA	On-Site Inspection Agency
POW/MIA	Defense Prisoner of War/ Missing in Action Office
SOC	Special Operations Command
USUHS	Uniformed Services University of the Health Sciences

Appendix H. General Ledger Control and Financial Reporting Weaknesses (KAR 1)

Defense agencies must have an accounting system that contains general ledger control and that maintains an appropriate account structure approved by the DoD. However, general ledger and financial reporting material weaknesses existed at the accounting offices that support 22 Defense agencies.

Inspector General, DoD, Report No. 97-017, "Consolidated FY 1995 Financial Report on Defense Organizations Receiving Department 97 Appropriations," October 31, 1996. The accounting organizations supporting 19 of 29 Defense organizations submitted adjusted FY 1995 trial balances to the DFAS Indianapolis Center from sources other than a complete general ledger accounting control system (see the table below). As a result, about \$19 billion of Department 97 funding was not controlled through a complete general ledger control system. Additional audit reports of three Defense agencies also disclosed specific KAR 1 weaknesses.

Accounting Systems That Had Incomplete General Ledger Control Systems

Defense Agency	System
American Forces Information Service	Navy/Air Force
Ballistic Missile Defense Organization	Navy/Air Force
Defense Acquisition University	DBMS ¹
Defense Advanced Research Projects Agency ²	Navy/Air Force
Defense Contract Audit Agency	DBMS
Defense Information Systems Agency	Navy/Air Force DBMS
Defense Investigative Service	Air Force
Defense Logistics Agency ²	DBMS
Defense Mapping Agency ³	Air Force
Defense Medical Program Activity	Air Force/Navy
Department of Defense Education Activity	Navy/FCS ⁴
Federal Energy Management Program	Navy/Air Force
Joint Staff	Navy/Air Force
Office of Civilian Health and Medical Program of the Uniformed Services ²	RAMS ⁵
Office of the Secretary of Defense	Navy/Air Force
	CUFS ⁶ /FCS/DBMS
Office of Economic Adjustment	Air Force

See footnotes on the next page.

Appendix H. General Ledger Control and Financial Reporting Weaknesses (KAR 1)

Accounting Systems That Had Incomplete General Ledger Control Systems (Cont'd)

Defense Agency	System
Special Operations Command	Navy/Air Force
Uniformed Services University of the Health Sciences	CUFS
Washington Headquarters Services	Navy/Air Force FCS/DBMS

¹Defense Business Management System.

²KAR 1 weakness also presented in an additional report, summarized below.

³Now the National Imagery and Mapping Agency.

⁴Fund Control System.

⁵Resource Accounting Management System.

⁶College and University Finance System.

Army National Guard. The Army National Guard does not have an accounting system with general ledger control. The Army National Guard applies a computer program to its budget execution system to derive general ledger accounts. In addition, the Army National Guard does not have transaction-based subsidiary ledgers, inappropriately used a real property account to record military equipment acquisitions, and inappropriately recorded allotted authority in a Defense Business Operations Fund account. As a result, the Army National Guard general ledger accounts contained misstatements for asset, liability, and budgetary accounts.

Army Reserve. The DFAS Indianapolis Center prepares trial balances for Defense agencies and the Army Reserve. The Army Reserve provided the DFAS Indianapolis Center with general ledger data. However, the DFAS personnel omitted Army Reserve financial data for FYs 1992 through 1995 because DFAS Indianapolis Center personnel did not program their accounting system to extract that financial data. As a result, the Army Reserve Trial balance for FY 1995 was understated by \$70.1 million.

Defense Advanced Research Projects Agency. In FY 1995, DARPA suballocated about \$1.2 billion of its budget to the Army, Navy, Air Force, and various Defense agencies. The WHS performed the accounting function for 51 percent of those funds. The DFAS Centers at Indianapolis (Army), Cleveland (Navy), and Denver (Air Force) and the NSA accounting organization performed the accounting function for the remaining 49 percent. However, the accounting organizations supporting the Office of Naval Research and other Navy organizations, the Air Force, and the NSA did not submit adjusted trial balances to the DFAS Indianapolis Center. As a result, the FY 1995 DARPA trial balance was understated by at least \$697 million.

The DFAS Cleveland Center is developing a complete general ledger accounting control system, the Standard Accounting and Reporting System Fund

Appendix H. General Ledger Control and Financial Reporting Weaknesses (KAR 1)

Distribution and Departmental Reporting System, for the Navy to use. DFAS Cleveland System development managers estimated full implementation of the system by October 1996.

The Air Force selected the Corps of Engineers Financial Management System to account for Department 97 General Funds for the DFAS Denver Center. DFAS Denver Center personnel estimated full implementation of the system by December 1999.

Defense Logistics Agency. The FY 1995 DLA trial balance, prepared by the DFAS Columbus Center, contained imbalances totaling \$543 million between the general and supporting subsidiary ledgers and imbalances totaling \$894 million between equivalent proprietary and budgetary general ledger accounts, which were not reconciled. The DFAS Columbus Center did not reconcile the FY 1995 DLA general ledger because the Center's accounting system did not readily allow reconciliation.

The DFAS Columbus Center prepares the DLA financial statements and is responsible for maintaining the DLA general ledger accounts that support the financial statements. However, the DFAS Columbus Center did not prepare reliable FY 1995 financial statements for three DLA General Fund appropriations. Specifically, the supporting notes to the financial statements did not provide full disclosure for the Fund Balance with Treasury account. The notes did not disclose differences between summary disbursement and collection reports to the Department of the Treasury and DLA general ledger accounts.

In addition, the DFAS Columbus Center improperly used budget execution reports as data sources for three account balances reported on the three DLA General Fund statements. The DFAS Columbus Center managers believed that three general ledger account balances were unreliable and approved the use of budget execution reports as source data for the Accounts Receivable, Accounts Payable, and Revenue From Services Provided accounts. However, the amounts on the budget execution reports were different from the amounts shown in the DLA general ledger accounts.

National Security Agency. The NSA uses the General Accounting and Reporting System to perform planning, budgeting, accounting, and financial reporting, but the NSA had not programmed the system to produce trial balances for proprietary accounts by annual appropriations and allocation limit codes. Also, the NSA had not established an Appropriated Capital Used account in the system.

Office of the Civilian Health and Medical Program of the Uniformed Services. The OCHAMPUS did not establish and maintain adequate subsidiary accounts in the general ledger. OCHAMPUS established one subsidiary ledger and no subsidiary accounts to support one of multiple categories of Refunds Receivable, Case Recoupments Due to OCHAMPUS. In addition, OCHAMPUS did not reconcile that account to the general ledger Refunds Receivable balance. The OCHAMPUS accounting system did not perpetuate

Appendix H. General Ledger Control and Financial Reporting Weaknesses (KAR 1)

the balances of equipment and depreciation accounts from the end of one fiscal year to the beginning of the next, but reopened the accounts at the beginning of the next fiscal year under the new funding year accounting code.

The OCHAMPUS accounting staff submitted the FY 1995 financial data to the DFAS Indianapolis Center inappropriately using budgetary accounts as the data source for the Appropriated Capital Used account. The OCHAMPUS accounting staff manually calculated the Appropriated Capital Used account balance, but did not completely document or support the methodology they used to arrive at the account balance.

Appendix I. Property and Inventory Accounting Weaknesses (KAR 2)

We identified material property and inventory accounting weaknesses at the Army National Guard, DARPA, DIA, DLA, Department of Defense Education Activity, DTSA, NSA, the Office of the Secretary of Defense, and OCHAMPUS.

Army National Guard. The FY 1995 Military Equipment account reported for the Army National Guard included equipment items that did not meet Army equipment capitalization thresholds. Consequently, the Military Equipment account was overstated by about \$9.1 billion.

Also, the Army National Guard duplicated reporting of military equipment since the Guard maintained two separate methods of recording the equipment. The Army National Guard used property book records to report the on-hand value of military equipment. In addition, the Army National Guard recorded equipment acquisitions for the National Guard and Reserve Equipment Appropriation in its general ledger system upon the disbursement of funds. Consequently, \$427.1 million of National Guard and Reserve Equipment Appropriation military equipment was reported twice by the Army National Guard.

Defense Advanced Research Projects Agency. The Military Equipment account in the FY 1995 adjusted trial balance was understated by at least \$48 million. Four DARPA research organizations did not report the value of equipment purchased under DARPA suballocations. In addition, the WHS did not have supporting documentation for \$1.6 million of \$1.7 million of Military Equipment for the DARPA FY 1996 adjusted trial balance.

Defense Intelligence Agency. The DIA equipment account information reported to the DFAS Indianapolis Center for the FY 1995 financial statements was incorrect. The cost of capitalized equipment recorded in the general ledger and subsidiary property records was inaccurate because DIA did not use DoD capitalization criteria, included equipment purchased for other DoD Components, did not reconcile equipment property records to the general ledger, and did not include the cost of Government-furnished property to contractors. Also, DIA did not use DoD capitalization criteria when reporting the equipment balance to the DFAS Indianapolis Center for FY 1995. In addition, the DIA general ledger did not include equipment purchased prior to FY 1994. As a result, the DIA FY 1995 financial information is not reliable for financial reporting purposes.

Defense Logistics Agency. The DLA FY 1995 yearend General Fund Equipment account balance of \$411 million was materially misstated. The account was misstated because the DFAS Columbus Center did not make appropriate accounting entries at year's end to delete Defense Business Operations Fund equipment from the DLA General Fund Equipment account. The DFAS Columbus Center used the Defense Business Management System to roll up account balances on a daily basis, which causes difficulty in identifying

Appendix I. Property and Inventory Accounting Weaknesses (KAR 2)

assets in the individual reporting organizations. In its Annual Statement of Assurance, the DFAS Columbus Center reported the condition as a material noncompliance with KAR 2.

Department of Defense Education Activity. The Department of Defense Education Activity oversees the functions of the DoD Dependents Schools and the Domestic Dependent Elementary and Secondary Schools. The DoD Dependents Schools improperly accounted for about \$30.3 million of \$110.7 million of accountable property. Accountable property included in the official property records did not exist at DoD Dependents Schools-Europe sites, the official property records were not complete, the DoD Dependents Schools-Europe Supply Branch official property records on the location of accountable property were inaccurate, and the recorded values for accountable property were inaccurate.

In addition, the DoD Dependents Schools-Europe Area Superintendent approved incomplete and inaccurate reports of survey for losses of accountable property. Consequently, the DoD Dependents Schools-Europe did not hold employees accountable for property losses, totaling \$8.4 million during FY 1995, and did not detect all or correct underlying system problems.

Also, the DoD Dependents Schools Automated Material Management System, as implemented, did not effectively account for property. The Department of Defense Education Activity did not implement that system with the controls needed to prevent the recording of inaccurate data. The system permitted entries without supervisory approval or comments. Those entries included incomplete and duplicate records, zero and excessive valuation of property, and mass deletions of accountable property records.

Defense Technology Security Administration. For FY 1995, the DTSA Equipment in Use general ledger account was overstated by \$1.4 million for equipment that should have been expensed and by \$0.2 million for equipment that was no longer in use. The DTSA Equipment in Use account was overstated because the WHS Allotment Accounting System did not distinguish capital equipment acquisitions from noncapital equipment acquisitions on a unit cost basis. Noncapital equipment acquisitions are acquisitions that do not meet the current year capitalization threshold and, therefore, are charged as operating or program expenses. Additionally, the DFAS Indianapolis Center did not remove the value of disposed of equipment from the appropriate general ledger accounts. As a result, the DTSA FY 1995 Equipment in Use account, reported as \$5.2 million on the DTSA FY 1995 trial balance, is of limited use for financial management purposes.

National Security Agency. Equipment, real property, and inventory balances recorded in the NSA general ledger were incorrect, misstated, or could not be supported.

- o The NSA General Accounting and Reporting System was not programmed to record equipment purchases in accordance with the DoD capitalization threshold, and equipment accounts in the general ledger were not

Appendix I. Property and Inventory Accounting Weaknesses (KAR 2)

reconciled with subsidiary records. Also, equipment turned in to the Defense Reutilization and Marketing Service continued to be reported in the NSA general ledger.

- o As of March 31, 1996, property book records totaled only 72 percent of the balance in the general ledger real property accounts and NSA had not established procedures to reconcile the general ledger real property accounts to the property books.

- o The NSA General Accounting and Reporting System trial balance included items in inventory that either were misstated or could not be supported. For example, the March 31, 1996, inventory balance included \$14.6 million in an inventory account that had not changed since FY 1992. NSA personnel could not produce supporting documentation to show how the balance was derived. The March 31, 1996, trial balance also omitted two inventory management programs that the NSA accounting office was unaware of. As a result, the general ledger could not be relied on for information necessary to produce accurate financial statements.

Office of the Secretary of Defense. The DoD Components capitalized and retained in the financial records low-cost items that were below the current capitalization threshold. The DoD required Defense agencies and Military Departments to capitalize military equipment assets using varying thresholds. The DoD capitalization threshold has changed six times from a \$1,000 threshold in 1985 to a \$100,000 threshold in 1996. The DoD required that Defense agencies and Military Departments retain the capitalized amount of an equipment asset at the time it was purchased rather than apply the current capitalization threshold to all equipment assets, regardless of purchase date. As a result, the \$9.6 billion value of Department 97 Military Equipment Account reported for FY 1995 is of limited utility for financial management purposes.

Office of the Civilian Health and Medical Program of the Uniformed Services. The OCHAMPUS accounting staff improperly accounted for property by recording additions of property, valued at \$329,894, by increasing the Property account and the Appropriated Capital Account. The Appropriated Capital account is the proprietary Equity account used to record the use of the funds that Congress makes available. The amounts recorded in this account include appropriations and withdrawals. Additions of property normally should be recorded by increasing the Property account and either the Accounts Payable or Funds Disbursed accounts.

In addition, the OCHAMPUS accounting staff misclassified its \$2.7 million in computer equipment, \$2.5 million in accumulated depreciation, and \$0.3 million in depreciation expenses. The OCHAMPUS accounting staff recorded computer hardware and computer software in the Automated Data Processing Software account instead of the Equipment in Use account; accumulated depreciation in the Amortization of Leasehold Improvements and

Appendix I. Property and Inventory Accounting Weaknesses (KAR 2)

Other Intangible Assets account instead of the Accumulated Depreciation on the Military Equipment account; and depreciation expense in the Automated Data Processing Software account instead of the Depreciation of Equipment account.

Also, the OCHAMPUS staff incorrectly accounted for computer equipment in the Operation and Maintenance records instead of Procurement records, even though OCHAMPUS purchased the equipment with Procurement funds.

Appendix J. Accrual Accounting (KAR 5)

Material accrual accounting weaknesses existed at the DIA, NSA, and OCHAMPUS.

Defense Intelligence Agency. The DIA did not accrue liabilities for funds appropriated during FY 1994 and subsequent years because the DIA used the NSA accounting system, which had been programmed to automatically accrue liabilities only when disbursements were recorded. Also, accounts payable for funds appropriated prior to FY 1994 were not reliable because DIA recorded liabilities before receiving invoices and did not perform required followup on unpaid accounts payable. In addition, DIA had not established procedures to record accrued payroll and unfunded annual leave liabilities in the accounting system. As a result, the financial information produced and reported by DIA cannot be relied on to prepare accurate financial statements.

National Security Agency. Except for accruals of travel expenses and purchases of supplies through the DoD supply system, the NSA did not accrue expenses and liabilities until it made disbursements. Also, procedures had not been established to record the accrued, unfunded annual leave liabilities and the reported liabilities for travel-related expenses were overstated. As a result, the general ledger could not be relied on for the information necessary to produce reliable financial statements required by the Chief Financial Officers Act.

OCHAMPUS. The OCHAMPUS did not correctly account for the accrual of direct and part of the reimbursable program expenses. The Chief, Finance and Accounting Branch, stated that the OCHAMPUS did not have adequate time and personnel to perform that function.

Appendix K. System Controls (Fund and Internal) (KAR 7)

Material system controls weaknesses existed at the DARPA, Department of Defense Education Activity, DFAS Columbus Center, and OCHAMPUS.

DARPA. The DARPA FY 1995 trial balance did not accurately present the actual activity of the Printing and Reproduction and Transportation of Things expense accounts. The Printing and Reproduction account showed a negative balance of \$218,303, while the actual FY 1995 expense was \$14,867. The Transportation of Things account showed a negative balance of \$16,284, while the actual FY 1995 expense was \$6,243. Both negative balances resulted from a correction of prior years' balances of funds that had been obligated, but never disbursed.

Department of Defense Education Activity. The Department of Defense Education Activity manages and supervises the Domestic Dependent Elementary and Secondary Schools and the DoD Dependents Schools. The Domestic Dependent Elementary and Secondary Schools used \$5.4 million of FYs 1993 through 1996 Operation and Maintenance funds, rather than Procurement funds, to acquire and install capital equipment and software for their local area networks. Also, from FYs 1994 through 1996, the DoD Dependents Schools used at least \$1.5 million of Operation and Maintenance funds, rather than Procurement funds, to acquire and install local area networks at 10 schools in the Pacific region. In addition, the aggregate cost of the local area networks acquired with Operation and Maintenance funds exceeded the dollar thresholds Congress established for the use of Operation and Maintenance funds.

DFAS Columbus Center Support for DLA. The DFAS Columbus Center did not perform quality control reviews of three DLA General Fund statements to confirm the accuracy of the reported account balances. The DFAS Columbus Center erroneously included the costs for DoD civilian benefits in the Benefit Program Expenses account rather than the Operating and Program Expenses account. The DFAS Columbus Center also erroneously made manual entries to record the accrued liability for unfunded annual leave in the Cumulative Results of Operations account and Operating and Program Expenses account.

OCHAMPUS. The OCHAMPUS uses the Resource Accounting Management System to record and report financial information. That system did not accurately record the reimbursable obligation authority in the Allotted Reimbursable Program account because the accounting system did not register the results of the transactions to record the reimbursable obligation authority. In addition, OCHAMPUS reported a negative balance of \$1.07 billion in the Allotted Reimbursable Program account at September 30, 1995, and a negative balance at the end of the 12 months in that fiscal year. As a result, the OCHAMPUS accounting records were not reliable.

OCHAMPUS also reported a negative Fund Balance with Treasury of \$194 million for FY 1994 and \$298 million for FY 1995. OCHAMPUS paid

Appendix K. System Controls (Fund and Internal) (KAR 7)

for CHAMPUS health care costs before receiving reimbursement from the Military Departments. As a result, the OCHAMPUS may have violated the Antideficiency Act.

The OCHAMPUS management needed to either initiate or improve internal controls over financial accounting and reporting. Improvements are needed in the following areas.

- o OCHAMPUS management had not clearly assigned responsibility for creating and maintaining all subsidiary accounts.
- o The same manager was responsible for authorizing payments, and processing, recording, and reviewing accounting transactions at OCHAMPUS.
- o No manager or supervisor reviewed the Report on Financial Position prepared by the manager who was responsible for authorizing payments and for processing, recording, and reviewing accounting transactions at OCHAMPUS.
- o OCHAMPUS personnel had not been adequately trained in general ledger and trial balance preparation.
- o OCHAMPUS did not have written procedures for preparing reportable financial data.
- o OCHAMPUS accounting staff did not promptly correct irregularities that were identified in the accounting records, procedures, or system.

Also, OCHAMPUS did not take action to provide reasonable assurance that the Resource Accounting Management System accurately showed funds availability. OCHAMPUS also did not have procedures to ensure that the reimbursable program properly recorded the receipt of Military Interdepartmental Purchase Requests and non-DoD orders and the corresponding fund obligations.

Appendix L. Correction of Material Accounting System Weaknesses

Defense agencies have taken aggressive actions to correct material accounting system weaknesses identified during audits of Defense agencies' FY 1994 financial statements. Inspector General, DoD, Report No. 97-008, "FY 1994 Financial Statement Audits of Defense Agencies," October 25, 1996, summarizes accounting system weaknesses identified during the audits, the recommendations for corrective action, and the initial client responses to the recommendations. This appendix discusses the corrective actions.

General Ledger Control and Financial Reporting Weaknesses

Defense Advanced Research Projects Agency. The DFAS, which prepared the DARPA financial statements, agreed to require all organizations that receive funding from DARPA to submit their trial balances to the DFAS DAO/WHs for consolidation. That action will permit DFAS to prepare DARPA financial statements from proprietary general ledger account balances.

Defense Information Systems Agency. The DISA issued an operating procedure to ensure that general ledger accounts, and not budget execution data, are used to prepare financial statements. The DISA also made prior period adjustments totaling \$9.1 million to correct erroneous transactions and requested that WHs add accounts to the DISA general ledger account structure to permit correct posting of certain future transactions. However, the DISA also stated that it could not implement the corrective actions for its field organizations. See the discussion on this issue in Appendix M.

Defense Special Weapons Agency. The Defense Special Weapons Agency (DSWA) (formerly the Defense Nuclear Agency) initiated an accounting system change to create a consolidated general ledger trial balance report. In addition, the DSWA corrected the existing accounting system program to add account 5700, Appropriated Capital Used, to its general ledger account structure and made other programming changes to permit annual closing of revenue and expense accounts to equity accounts, and to correct balances accumulated in its Fund Balance with Treasury and its Equity accounts.

Corporate Information Management. The Office of the Assistant Secretary of Defense (Command, Control, Communications, and Intelligence) implemented procedures to ensure that all allocations for the Corporate Information Management fund were reported in the Corporate Information Management trial balance and that the entire Corporate Information Management allocation was processed by a single accounting system, the WHs Allotment Accounting System. That system generates general ledger-based trial balances used to prepare required financial statements.

Appendix L. Correction of Material Accounting System Weaknesses

On-Site Inspection Agency. The On-Site Inspection Agency uses the same accounting system as the DSWA and, therefore, was subject to the same material accounting system weaknesses as the DSWA. Accordingly, the accounting system and programming changes initiated by DSWA will also correct the On-Site Inspection Agency material weaknesses.

Property and Inventory Accounting Weaknesses

Defense Special Weapons Agency. The DSWA corrected computer logic errors and developed subsidiary ledger programs to correct military equipment reporting deficiencies affecting a reported military equipment balance of \$463.6 million. The DSWA also initiated action to conduct an inventory of its military equipment, reconcile the results with general ledger account balances, and make any necessary adjustments. Additionally, the DSWA took steps to determine ownership of military equipment assets provided to the Republics of the former Soviet Union under the Cooperative Threat Reduction Program and to adjust the military equipment accounts to reflect only assets owned by the DSWA.

Defense Mapping Agency. The DMA (now the National Imagery and Mapping Agency) agreed to perform a complete inventory and update its property and inventory records and to perform annual random sample inventories. That action will be deferred for an indefinite period, pending a relocation of inventory and installation of a new inventory system, the Job Order Cost Accounting System II, as discussed in Appendix M. The DMA also agreed to establish inventory accountability procedures and controls and to train its personnel in those procedures and controls.

Defense Information Systems Agency. The DISA completed corrective actions and stated that it would take other actions that are or will be responsive to the audit report recommendations. Specifically, DISA:

- o removed military equipment, valued at \$1.6 million and transferred to another agency, from the DISA military equipment account and notified that agency of the need to record the equipment in its accounts;
- o requested that WHS add accounts, required for proper financial reporting, to the DISA general ledger account structure maintained in the WHS Allotment Accounting System, the system DISA uses for its accounting and financial reporting;
- o made prior period adjustments to remove from the military equipment accounts equipment items valued at \$0.4 million that should have been expensed in FY 1995;
- o made prior period adjustments to reclassify military equipment valued at \$7.1 million that should have been recorded as Automated Data Processing Software; and

Appendix L. Correction of Material Accounting System Weaknesses

- o initiated action to review and update DISA property accountability procedures and issue revised guidance.

The DISA also stated that after transferring property records to the Defense Property Accountability System, DISA would reconcile its property records and make appropriate accounting entries to properly classify its military equipment, as discussed in Appendix M.

Washington Headquarters Services. The WHS took action during the audit to:

- o reclassify furniture and other items in the Military Equipment account, valued at \$9.5 million, that should have been expensed; and

- o correct an error in the WHS Allotment Accounting System that improperly capitalized, in the WHS Military Equipment account, assets valued at \$1.9 million that were purchased for other entities.

Controls Weaknesses (Fund and Internal)

Defense Advanced Research Projects Agency. The DFAS stated that it would implement the DoD management control program at the accounting organization that supports DARPA and include the results of management control program reviews in the FY 1996 DFAS Denver Center Annual Assurance Statement.

Ballistic Missile Defense Organization. The DFAS corrective action response, with respect to the DARPA general ledger control weakness, is also applicable to the Ballistic Missile Defense Organization because:

- o DFAS also performs accounting services for the Ballistic Missile Defense Organization, and

- o the audit identified similar weaknesses in the Ballistic Missile Defense Organization financial statements.

Joint Staff. The DFAS corrective action response, with respect to the DARPA general ledger control weakness, is also applicable to the Joint Staff because:

- o DFAS also performs accounting services for the Joint Staff and

- o the audit identified similar weaknesses in the Joint Staff financial statements.

Defense Information Systems Agency. The DISA issued a new requirement to perform annual accounting system reviews to ensure that its new procedures to use the DoD general ledger proprietary account structure worked as intended.

Audit Trail Weaknesses

The DFAS established controls to ensure that supporting documentation be filed in a timely manner and maintained in a centralized and readily accessible location. The corrective actions will result in improved audit trails for transactions processed by the following Defense agencies, for which DFAS performs installation accounting functions:

- o American Forces Information Service,
- o Ballistic Missile Defense Organization,
- o Defense Advanced Research Projects Agency,
- o Defense Legal Services Agency,
- o Defense Medical Programs Activity, and
- o Joint Staff.

Appendix M. Previously Reported Material Accounting System Weaknesses Requiring Correction

Despite the improvements discussed in Appendix L, significant weaknesses still remain in Defense agency accounting systems. Actions required to correct the following material weaknesses were delayed to subsequent fiscal years or specific implementation dates for corrective action could not be provided or did not correct the weaknesses.

General Ledger and Financial Reporting Weaknesses

Defense Information Systems Agency. Although DISA issued new operating procedures to ensure that general ledger accounts are used to prepare financial statements, DISA field organizations were still not using the automated general ledger of the WHS Allotment Accounting System. DISA estimated that full implementation of the new procedures at the field activities will not occur until FY 1998 at the earliest, because DISA may utilize a different accounting system in FY 1998 and because further implementation of the current system would not be cost-effective.

WHS maintains the DISA general ledger structure in the WHS Allotment Accounting System. On July 11, 1996, the DAO/DISA requested that WHS add accounts to the DISA general ledger structure to permit DISA reclassification of certain military equipment assets as Equipment with Contractors (account 1763) Equipment on Loan (account 1764), and Capitalized Computer Software (account 1830). However, WHS did not add accounts 1763 and 1764 to the DISA general ledger, but a WHS official stated that WHS planned to do so by December 31, 1996.

Defense Advanced Research Projects Agency. We recommended that the DFAS implement a continuing professional education program for the accounting technicians who perform accounting services for DARPA. The accounting personnel who prepared the financial statements had received no training on financial statement preparation and as a result, prepared the statements from budget execution data instead of proprietary general ledger account balances. The DFAS Denver Center agreed to provide one-time training to its accounting technician personnel in the use of the DoD standard general ledger, but did not implement a recommended continuing professional education program, because the DFAS believed the one-time general ledger training would be sufficient. One-time training may provide accounting technicians with the knowledge to comply with current requirements, but does not ensure that technicians stay abreast of changes in accounting requirements.

Appendix M. Previously Reported Material Accounting System Weaknesses Requiring Correction

Other Defense Agencies. DFAS DAO/WHS accounting technicians also perform accounting services and prepare financial statements for other Defense agencies. Inspector General, DoD, Report No. 96-048, "Defense Accounting Office, Washington Headquarters Services, Procedures for Preparing FY 1994 Financial Statements for the Advanced Research Projects Agency," December 19, 1995, identifies the other Defense agencies as the Ballistic Missile Defense Organization, the Joint Staff, and the Office of the Inspector General, DoD. As discussed in this appendix, with respect to the DARPA financial statements, the recommended continuing professional education program will be more effective than one-time training to ensure that accounting technicians maintain the skills necessary to prepare financial statements.

Property and Inventory Accounting Weaknesses

Defense Information Systems Agency. The DISA materially overstated its Equipment in Use account because DISA did not properly analyze military equipment transactions. Although the DISA has taken significant corrective actions and agreed to reconcile its property records and transfer the property accountability function to the DoD Property Accountability System, DISA still needs to convert its property accounting to the Defense Property Accountability System. That system will provide centralized property accountability and obtain data from property custodians' records and will interface with the financial accounting system to be used by DISA. The DoD Property Accountability System will provide DISA with better visibility of its property and will facilitate accurate recording and classification of future acquisitions. DISA has not yet completed the conversion to the DoD Property Accountability System and did not provide an estimated completion date. In addition, DISA may move its financial accounting to another accounting system in FY 1998. The new system will interface with the DoD Property Accountability System.

Defense Mapping Agency. Although the DMA (now the National Imagery and Mapping Agency) established inventory accountability procedures and controls, the DMA will not be able to take the following agreed-upon corrective actions until FY 1998 at the earliest.

- o Perform a complete inventory of DMA mapping, charting, and geodesy products, and follow up with annual random sample inventories.
- o Use historical costs to value inventory, pending implementation of the Job Order Cost Accounting System II.
- o Adjust unit costs as necessary, pending implementation of the Job Order Cost Accounting System II.
- o Include a footnote in future financial statements to identify the estimated amount of inventory in excess of anticipated requirements and required war reserves.

Appendix M. Previously Reported Material Accounting System Weaknesses Requiring Correction

The DMA plans to defer action until FY 1998 or later because it needs to relocate its inventory to a new site and implement new inventory and cost accounting systems.

Washington Headquarters Services. The WHS agreed to establish controls to ensure that assets are properly capitalized and presented in financial statements. WHS agreed to apply one capitalization threshold to all DoD asset accounts within 60 days of a decision by the Under Secretary of Defense (Comptroller) on whether to adopt the recommendations regarding the capitalization threshold in Inspector General, DoD, Report No. 96-212, "Capitalization of DoD General Property, Plant, and Equipment," August 19, 1996.

Inspector General, DoD, Report No. 96-212, "Capitalization of DoD General Property, Plant, and Equipment," August 19, 1996, recommends that the Chief Financial Officer direct the DoD Components to apply one capitalization threshold to general property, plant, and equipment accounts and to adjust financial records accordingly. The Comptroller generally concurred with the report recommendation and is taking action to change the DoD capitalization threshold.

Appendix N. DoD Initiatives

Program Budget and Accounting System. The Program Budget and Accounting System, currently used by the Army, is intended to correct and prevent discrepancies, such as problem disbursements and abnormal fund balances, by controlling the funds distribution process at all organizational levels. The original implementation date at Defense agencies for the Program Budget and Accounting System was October 1, 1996. However, the system entered a 2-month test phase at the Defense agencies on October 1, 1996. The Under Secretary of Defense (Comptroller) plans to implement the Program Budget and Accounting System at Defense agencies in December 1996, following the test period.

DoD Property Accountability System. On December 22, 1994, the Under Secretary of Defense (Comptroller) selected the DoD Property Accountability System as the migratory¹ system for all DoD property, including military equipment. That system will replace the current inventory of property accountability and accounting systems and will include asset data, such as acquisition dates and costs, required for adequate financial reporting of property not included in many existing systems. The DoD Property Accountability System will interface with financial accounting systems and will post information to the system as a by-product of the property custodian's accountability processes. Those improvements, when implemented, will correct existing systemic property accounting and reporting weaknesses. The initial target date for DoD-wide implementation of the DoD Property Accountability System was September 1997. However, Military Department implementation has slipped until September 2000, because the use of multiple migratory accounting systems resulted in the need for developing more interfaces than initially anticipated. The current DFAS milestone for completing the implementation of the DoD Property Accountability System at the Defense agencies is still September 1997.

Chief Financial Officers Financial Statements. In FY 1996, the DFAS Indianapolis Center assumed responsibility for preparing financial statements for the Defense agency appropriations. The DFAS Indianapolis Center will accomplish this task by having Defense agency accounting offices submit monthly trial balances for updating the general ledger. This initiative will result in a more current general ledger and will facilitate a smoother fiscal yearend closing and reporting process. The level of reporting detail will be sufficient to show the agency and appropriation, with details available at the fiscal station level. However, recent audit reports (as summarized in Appendix C) disclosed material weaknesses in the processing of financial data submitted by Defense agencies and recommended that corrective actions be taken by the DFAS Indianapolis Center.

¹An existing or planned and approved automated information system that has been designated to support a functional process on a DoD-wide basis.

Standard Finance and Accounting Systems. The DFAS concept for future operations includes improving, modifying, and implementing standard migratory finance and accounting systems throughout DoD. DFAS plans to achieve a rapid reduction in the number of accounting systems by selecting interim migratory systems to replace legacy² systems. DFAS implemented this incremental approach to reduce the risks and costs of developing new systems. With this strategy, DFAS intends to overcome fundamental accounting problems such as the lack of:

- o a standard general ledger,
- o common budget and accounting classification codes,
- o adequate costing methods,
- o full property accounting, and
- o adequate documentation.

The Federal Financial System process used at the DFAS Indianapolis Center to receive, adjust, and consolidate general ledger trial balances will eventually be incorporated into a new system. However, Inspector General, DoD, Report No. 96-180, "The General Fund Interim Migration Accounting Strategy," June 26, 1996, states that the migration strategy selected by DFAS should be replaced with a more efficient strategy. The report states that the DFAS goal was to implement the strategy at the Indianapolis Center by September 1997. However, the strategy, which includes consolidation of DoD accounting offices, will not be complete for the DFAS Indianapolis Center until FY 1999 at the earliest, because of the time required to implement the designated new accounting system for the Indianapolis Center.

Consolidation of DoD Accounting Offices. The DFAS plans to reduce the number of sites that perform finance and accounting functions from 300 to 26 sites. The DFAS selected 6 of the 26 sites to function as operating locations for the DFAS Indianapolis Center, which performs accounting services for the Defense agencies. The DFAS Indianapolis Center, Chief Financial Officers Financial Management 5-year Plan, September 1995, projected that the consolidation would be completed during FY 1996. However, the consolidation of DoD accounting offices is part of the General Fund Interim Migration Strategy, and the consolidation is closely tied to selection of migratory accounting systems. As a result, a DFAS official stated that the consolidation of DoD accounting offices is unlikely to be completed before FY 1999.

²An automated information system that is a candidate for phaseout, upgrade, or replacement, usually because the system does not comply with data standards or other standards.

Appendix O. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition and Technology
Director, Defense Logistics Studies Information Exchange
Under Secretary of Defense (Comptroller)
 Deputy Chief Financial Officer
 Deputy Comptroller (Program/Budget)
Assistant Secretary of Defense (Command, Control, Communications, and Intelligence)
Assistant Secretary of Defense (Health Affairs)
Assistant Secretary of Defense (Public Affairs)
Director, Joint Staff

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, Ballistic Missile Defense Organization
Director, Defense Advanced Research Projects Agency
Director, Defense Contract Audit Agency
Director, Defense Finance and Accounting Service
Director, Defense Information Systems Agency
Director, Defense Legal Services Agency
Director, Defense Special Weapons Agency
Director, National Imagery and Mapping Agency
Director, National Security Agency
 Inspector General, National Security Agency
Director, Defense Technology Security Administration
Director, Department of Defense Education Activity

Other Defense Organizations (Cont'd)

Director, Office of Civilian Health and Medical Program of the Uniformed Services
Director, On-Site Inspection Agency
Director, Washington Headquarters Services
Inspector General, Defense Intelligence Agency

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 National Security, International Affairs, and Criminal Justice,
Committee on Government Reform and Oversight
House Committee on National Security

This page was left out of original document

Part III - Management Comments

Department of Defense Education Activity Comments

Final Report
Reference



DEPARTMENT OF DEFENSE
EDUCATION ACTIVITY
4040 NORTH FAIRFAX DRIVE
ARLINGTON, VIRGINIA 22203-1635



February 10, 1997

MEMORANDUM FOR DIRECTOR, READINESS AND OPERATIONAL SUPPORT
DIRECTORATE, INSPECTOR GENERAL, DOD
(ATTN: MR. THOMAS F. GIMBLE)

SUBJECT: Management Response to the Draft of a Proposed Audit Report, "Material Accounting and Management Control Weaknesses in the Defense Agencies' FY's 1995 and 1996 Financial Information," Project No. 6RA-2014.03, December 31, 1996

Thank you for providing the Department of Defense Education Activity the opportunity to review the subject draft report. We would like to share a few observations and comments.

We do not agree with the use of information upon which a consensus has not been drawn in the manner presented in the subject draft audit report. Repeatedly stating a position as factual, when in reality it is in contention, significantly detracts from the value of the audit.

The subject draft report draws its conclusions from eighteen audit reports, prepared by the Inspector General, DoD. Among the eighteen reports, three were in regard to the administration and operations of the DoDEA. From those three reports, the DoDEA is mentioned, or referenced fifteen times in the draft report. None of the references to DoDEA make mention of the corrective actions that were underway prior to or during the audit period.

In particular, the draft report references three audit reports of DoDEA as the basis for determining, evaluating, and summarizing the DoDEA's accounting systems and management controls. The first of these reports was Department of Defense, Office of the Inspector General, Audit Report, "Report on Potential Antideficiency Act Violations at the Department of Defense Education Activity," Report No. 97-078 (Project No. 6LA-2011-03), January 23, 1997. The DoDEA generally concurred and has reported that they have taken action in regard to recommendations to discontinue the acquisition and installation of investment items with Operations and Maintenance funds and to obligate Procurement funds for the cost of investment items procured. However, DoDEA disagreed that Antideficiency Act violations would have occurred because it had Procurement funds to cover those accounting adjustments. Additionally, DoDEA disagreed with the definition of a system stating that the local area networks at the

Department of Defense Education Activity Comments

	Final Report Reference
2	
schools were individual stand alone systems, based on the primacy of purpose of each system. The references, below, would provide greater benefit if they reflected DoDEA's constructive and aggressive actions in regard to the weaknesses presented in the referenced report of audit. Page 6, a Fund Control Weakness. Page 7, an Internal Control Weakness. Page 22, a Potential Antideficiency Act Violation. Page 43, an Accounting System Weakness. Page 53, Material Systems Controls Weaknesses.	Page 6 Page 6 Page 21 Page 43 Page 53
The second referenced audit report of the DoDEA was Department of Defense, Office of the Inspector General, Draft of a Proposed Audit Report, "Property Accountability for the Department of Defense Education Activity," Project No. 6LA-2011, September 30, 1996. The September 30, 1996, report is identified in the subject draft audit report as a "draft" audit report, the final report (No. 97-082) was issued on January 28, 1997. In response to the findings and recommendations of this report the DoDEA expanded its strategic plan's focus to include property accountability. DoDEA has established quality review teams to ensure that equipment inventories are accurate and to develop a quality control program. DoDEA is distributing the reports of survey regulation to personnel, initiating reports of survey training, and has begun a quarterly review of all reports of survey to determine whether losses are investigated in an appropriate and timely manner. Because of DoDEA's geography, they will appoint five senior level officials as approving authorities for all reports of survey. DoDEA is taking action to modify the Dependents Schools Automated Material Management System to incorporate appropriate edit checks and eliminate the duplication of data entry. DoDEA is implementing a program to ensure that equipment acquisitions are equitably distributed within the organization. The references, below, do not reflect the aggressive and positive actions taken by DoDEA officials to rectify the conditions noted in the underlying audit report. Page 4, Material Property and Inventory Weaknesses. Pages 23 and 24, Property Accountability Weaknesses. Page 30, Management Control Weaknesses. Page 36, Adequacy of Controls for Property Accountability. Page 43, an Accounting System Weakness. Page 49, Property and Inventory Accounting Weaknesses.	Page 20 Page 4 Page 20 Page 31 Page 34 Page 43 Page 49
The third audit report of DoDEA referenced in the subject draft audit report was Department of Defense, Office of the Inspector General, Audit Report, "Management Control Environment for the Department of Defense Education Activity," Report No. 96-181, June 28, 1996. The following references to DoDEA based upon this audit report do not appropriately reflect the corrective actions pursued by management. Among these actions were the establishment of an independent internal review organization, modification to year-end spending procedures, improvements to accounting guidance, changes to improve the reliability of	Page 34

Department of Defense Education Activity Comments

Final Report
Reference

Page 30
Page 34
Page 44

Page 34

3

accounting reports, effecting property management controls, putting into use a general ledger, and continued emphasis on the importance of the Department of Defense Management Control Program. The subject draft audit report should appropriately include mention of the decisive and effective actions taken by DoDEA managers in response to the criticisms contained in the underlying audit report.

Page 30, Management Control Weaknesses.

Page 36, Adequacy of Controls for Property Accountability.

Page 40, Accounting Systems that had Incomplete General Ledger Control Systems.

The reference to Audit Report No. 96-181 (page 36 of the subject draft audit report), is in error when it states, "The DoD Education Activity did not include property accountability as an area requiring management's attention in its Annual Statement of Assurance, but nevertheless, initiated actions to improve the accuracy of accountable property reporting." Property accountability was reported in the DoDEA Annual Statement of Assurance as a subset of the material weakness reported for Equipment Management (DoD MC reporting Category No. 7, "Supply Operations"). Moreover, the weakness had been reported in some form in the DoDEA Annual Statement of Assurance since 1984.

We trust that these comments will be helpful to you in putting your report in final form. If we can provide any additional information, please do not hesitate to call me or Mr. Paul Goss at 696-9051, extension 4241.

for Paul Goss
SAMIH H. HELMY
Chief, Internal Review and
Audit Oversight Office

Audit Team Members

This report was prepared by the Readiness and Operational Support Directorate, Office of the Assistant Inspector General for Auditing, DoD.

Thomas F. Gimble
Salvatore D. Guli
Mary Lu Ugone
Karim Malek
Jonathan Rabben
Margaret Bennardo
Nancy Cipolla
Cristina Maria H. Giusti
Bernice M. Lewis

INTERNET DOCUMENT INFORMATION FORM

A . Report Title: Material Accounting and Management Control Weaknesses in the Defense Agencies FYS 1995 and 1996 Financial Information

B. DATE Report Downloaded From the Internet: 10/26/99

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** 10/26/99

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.