

**STRATEGY
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**IMPROVING MILITARY ACCOUNTING TO SUPPORT THE
MILITARY DECISION-MAKING PROCESS**

BY

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ABSTRACT

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DOD's accounting systems do not adequately document and report financial disbursements and military expenditures. The General Accounting Office and Defense Audit Agencies determined that significant accounting weaknesses exist and contribute to financial mismanagement, fraud, waste, and abuse of public funds. However, with the passage of the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, there are significant efforts ongoing to regain funds accountability to support our national defense interests and security. The creation of the Defense Finance and Accounting Service and a number of new financial and logistics information systems will provide faster responsiveness and reliability. Perhaps the overriding benefit of improving the military accounting systems is the potential savings that can be obtained and reallocated to readiness accounts from timely and reliable financial analysis. This analysis will determine where cost redundancies exist, identify potential cost overruns, reduce interest penalties to contractors, and signal additional savings in future Base Realignment and Closure Programs. Responsive and reliable accounting measures can identify additional monies for Military Readiness, Force Modernization and Quality of Life Programs. The use of new accounting methods such as Activity Based Accounting will support commanders and leaders to reduce overhead costs.

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IMPROVING MILITARY ACCOUNTING TO SUPPORT THE MILITARY DECISION-MAKING PROCESS

"I think it an object of great importance... to simplify our system of finance and bring it within the comprehension of every member of Congress."

—Thomas Jefferson, April 1802¹

Why is having accurate and timely accounting information important to Department of Defense decision-makers? The answer is summarized in four words: accountability, credibility, law, and savings. The American Congress is accountable to its constituents (the American people) to ensure that \$300 billion annual defense budgets are expended for their intended purposes. After years of neglect, the current government-wide accounting systems, and in particular, the Department of Defense (DOD) accounting systems are unreliable, unauditable, and incapable of fully authenticating military spending. These accounting systems must be credible to ensure that Congress has absolute confidence that monies allocated to support military programs for readiness, modernization, and the quality of life of DOD personnel are spent correctly and efficiently. A number of new laws and amendments were enacted during the past decade to increase the accountability and credibility of financial statements. The ability to use accounting to identify savings and cost redundancies has the greatest potential benefit for today's military decision-maker.

The Chief Financial Officers Act (Public Law 101-576) of 1990, as amended by the Federal Financial Management Act of 1994, requires financial statement audits by the Department of Defense Inspectors General.² With that stated, military and civilian leaders in today's Department of Defense must realize that their financial responsibilities do not end with the approval of the annual Future Years Defense Program as produced within the Planning, Programming, Budgeting, and System (PPBS). These leaders must ensure that in accordance with the Chief Financial Officers (CFO) Act, a thorough accounting and audit of those budgeted funds is necessary to ensure they were spent properly. Decision makers, throughout all levels of the Department of Defense, need timely and accurate financial information to aid in sound and prudent decisions. These decisions impact the amount of funds available for military readiness, quality of life, and future modernization programs.

This paper documents accounting weaknesses and financial reforms, along with emerging interoperable financial systems, designed to increase the reliability of accounting information. DOD's weak accounting systems impact critical decision-making processes regarding military readiness, the Quadrennial Defense Review (QDR), and Defense Base Realignment and Closure (BRAC) Commission. Improvements and enhancements to these

accounting systems will provide leadership with an important tool in the decision-making process.

BACKGROUND

In general, federal government accounting systems were designed to answer two masters: the internal senior manager or field commander and the external master of mandatory reporting to Congress (or the American Public). The federal government, including DOD, is considered a non-business organization and does not rely on accounting information for profit-oriented reasons. Consequently, accounting and financial analysis of the performance of DOD activities and organizations is considerably different than private industry or other revenue-producing entities. Nonetheless, reliable and timely accounting information can greatly assist senior civilian and military leaders in making decisions affecting the national security and readiness of the United States.

Since its formation in 1947, the DOD has largely consisted of decentralized sub-departments and operations. Decentralization of various military organizations and agencies proved extremely beneficial in maintaining readiness, promoting initiative and enhancing professional development. However, a drawback to these decentralized organizations is that in most cases they managed their own budget, finance and accounting systems. Consequently, as a result of these multiple systems, a variety of business and management practices evolved during the period.

As the management and design of military equipment, property and supplies became increasingly more complex, so did the accounting and financial systems that supported them. Such complexities led to increased errors based on the demands of the systems. In addition, the number of accounting organizations designed to track expenditures throughout the military services increased therein escalating the magnitude of accounting data. Until 1991, over 330 separate accounting offices existed throughout the Department of Defense.

The massive scope of DOD's operations is unparalleled in either the private or public sectors. The unique challenges that DOD encounters in managing such a huge and complex organization are compounded by its long-standing financial management weaknesses. Spending 50% of the federal government's discretionary spending, DOD's financial management problems result in a lack of accountability over a substantial portion of the government's financial resources. These problems have led to inaccurate information being provided to the Congress and the inefficient use and waste of resources.³

ACCOUNTING DEFINITIONS AND OBJECTIVES

Many senior leaders and managers would rather undergo a "root canal" than explore the causal relationships between accounting and military decision-making. Nevertheless, to bridge accounting to the military decision-making process, it is important to understand the meaning of accounting and some of its objectives. Simply put, accounting is the process of identifying, measuring, recording, and communicating financial information about an organization or entity.⁴ Within DOD, accounting establishes control over all assets provided to, or acquired by the Department of Defense. Assets remain under continuous accounting control from acquisition to disposition. These controls help maintain adequate accountability since no assets can be acquired, transferred, written off, or disposed of without the proper authorization necessary to document and record the transaction.⁵

A DOD Asset is any item of economic value owned by a DOD agency or component or held in a fiduciary capacity under the control of a DOD component. The value of a DOD asset is expressed in terms of its acquisition cost, and control of the asset by a particular DOD agency or organization must be the result of a past transaction or financial event.⁶

In addition to tracking military expenditures and disbursements, DOD accounting systems support control of appropriated funds, budget execution and reporting requirements. Due to the tremendous size of the user and support population in the Department of Defense, four categories of accounting systems exist to provide financial information. They include the following:

- Defense Working Capital Fund (DWCF) accounting systems support a wide spectrum of business operations within each of the military departments and defense agencies. This includes industrial (depot) operations, transportation, supply management, informational systems, financial transaction processing, research and development, and distribution depots.
- General Fund accounting systems support appropriated accounting in the military departments and defense agencies.
- Departmental accounting systems provide consolidated status reports to military departments and defense agencies, and the Office of the Secretary of Defense.
- Cash accountability systems report disbursement, reimbursements, deposit receipts to Treasury, and process cross-disbursement vouchers.

DISCUSSION

The need to eliminate organizational and information management weaknesses is imperative to realizing additional savings and recognizing efficiencies within the DOD. These savings and efficiencies can be reallocated to support Military Readiness Programs, Force Modernization Accounts, Congressionally-Directed QDRs and BRAC Commission Activities. In addition, accurate and timely accounting assists the DOD in requesting Congressional Supplemental Appropriations for Military Deployments. The following paragraphs explore the impact of accounting weaknesses on the overall financial management program and the improvements required to make financial analyses a part of the decision-maker "tool kit."

ACCOUNTING WEAKNESSES

The Department of Defense has been struggling to fix financial problems that are decades old. The financial management problems and weaknesses within the Department of Defense fall into the six following areas:⁷

- (1) Lack of an overall integrated financial management system structure.
- (2) Unreliable means of accumulating actual cost data to account for and manage resources.
- (3) Continuing problems in accurately accounting for billions of dollars in disbursements (problem disbursements).
- (4) Critical need to upgrade its financial management workforce and organizations.
- (5) Breakdowns in basic and rudimentary required financial control procedures.
- (6) Antiquated bureaucratic practices that underscore the need for progress in reengineering business practices.

Of the six financial problems stated above, the DOD's Inspector General singled out problem disbursements as a significant internal accounting problem. A problem disbursement occurs when expenditures are not reconciled with official accounting records. In Fiscal Year (FY) 1999, DFAS centers processed approximately \$7.6 trillion in department-level accounting entries.⁸ Of the \$7.6 trillion in department-level accounting entries, \$3.5 trillion were supported with proper research, reconciliation, and audit trails. However, \$2.3 trillion accounting entries required forced financial data reconciliation and did not contain adequate audit trails. Another \$1.8 trillion in accounting entries were not verified due to time constraints.⁹ The inability to properly reconcile accounting entries results in lost financial accountability and unauditable financial statements.

Beginning in 1991, the United States General Accounting Office (GAO) published a special review to report on federal program areas identified as high risk because of increased possibilities and vulnerabilities of waste, abuse, and mismanagement.¹⁰ In their review, the GAO pointed out that the Department of Defense needs accurate financial management information and better internal controls to manage the \$1 trillion in assets. Additionally, the report indicated that DOD's financial operations not only impair the reliability of financial information, but also result in wasted resources, and undermine the Department's ability to properly account for and oversee its resources and responsibilities.¹¹

In May 1999, William Lynn, the former Under Secretary of Defense Comptroller, testified to a Congressional House Budget Committee regarding financial management issues within the Department of Defense. In his testimony, Lynn indicated that financial management is important for three main reasons.¹²

- First, sound financial management practices provide visibility and oversight of costs. Determining how much the US Government pays for goods and services provides decision-makers, both senior managers and field commanders, with timely and accurate cost information needed to sustain maximum effectiveness. In addition, accurate cost information is necessary to the Department's ability to apply funds more precisely to modernization, training, and investments, and to assess performance and evaluate various programs.
- Second, sound financial management controls provide internal controls and safeguards to ensure those funds are spent for their intended purposes. These controls specify what was purchased and the quantities purchased before payments are made. Consequently, adequate and timely financial management controls discourage and prevent fraud, waste and abuse.
- Third, reliable financial operations support our troops. Providing accurate and timely payments to contractors and vendors from whom we obtain goods and services will ensure services remain available when and where we need them. In addition, dependable financial operations instill confidence in our military and civilian personnel that their financial entitlements, as well as their families will not be neglected even though they are sometimes assigned or deployed thousands of miles from home.¹³

Several legislative acts have been enacted to address and resolve accounting weaknesses. The Federal Accounting Standards Advisory Board (FASAB) was established in 1990 and charged with establishing a comprehensive set of accounting concepts and standards

for the federal government. In 1996, the Federal Financial Management Improvement Act established a mandate to implement and maintain financial management systems that comply with federal systems requirements, applicable federal accounting standards, and the standard accounting general ledger.¹⁴

GAO and Defense Audit Agencies have continuously pointed out that DOD's existing accounting and financial management systems are not integrated and lack a standard general ledger. An integrated general ledger system will provide the internal controls to accurately account for DOD's resources. In addition, the utilization of a standard general ledger will allow better interoperability with DOD's accounting, finance, logistics, personnel, and budgetary systems.¹⁵

MILITARY READINESS

Do these accounting weaknesses impact military readiness? Mr. Ernest Gregory, Deputy Assistant Secretary of the Army (Financial Operations), emphatically states that the lack of timely financial accounting has a direct impact on readiness.¹⁶ By properly accounting, analyzing and reporting financial information, senior leaders at all levels will be able to make informed decisions regarding the allocation of financial resources.

The United States places considerable emphasis on keeping its military forces prepared and ready to perform a wide-range of military operations. In a broad measure, military readiness can be defined as having a well trained, equipped and manned force. Some of the questions used to assess and gauge military readiness include: Are troops well trained? Do forces have enough spare parts, fuel, and ammunition to keep them operational? Is equipment in good repair? In most cases, the solutions to these questions include maintaining the visibility to track costs and cross-leveling existing financial resources to execute assigned missions. Managed carefully, seamless and interoperable financial systems can detect duplicate costs throughout the force and ensure funds are realigned. In his 1998 Annual Report to the President and the Congress, William Cohen, then Secretary of Defense, stated: "It is critical to note that successfully executing [our national] strategy requires that resources be reallocated from overhead and support our fighting forces. Failure to do so will threaten the readiness of our forces today and in the future."¹⁷

Despite the military's emphasis on readiness, it is difficult to estimate exactly how much money is spent on maintaining military readiness accounts. In fact, readiness is difficult to quantify, and to a certain extent, assessments depend on subjective military judgments.¹⁸ Producing timely and accurate financial statements will allow financial analysts and managers to

"peel back" the complex layers of large military programs and organizations to ensure manning, training, and equipping the force are conducted efficiently. Despite best intentions, cost overruns, high overhead, increased labor costs and delayed contractual payments add significantly to the cost of various programs which in turn absorb needed funds from readiness areas. Utilizing accounting information to assess cost trends and track cost variances will ensure leaders apply more resources to the right programs.

FORCE MODERNIZATION

The escalating costs of force modernization derive from the fact that each new generation of weapons is more complex and expensive than the generation being replaced. Proper use and analyses of accounting information ensures that senior leaders understand the complexities, potential financial risks, and embedded costs to enhance modernization programs.

For a number of years, the General Accounting Office has issued reports documenting how money is diverted from the procurement budget to the Operations and Maintenance (O&M) budget. This migration of procurement funds, as indicated in accounting reports, demonstrates that the rising cost of low readiness is overriding the attempt to shift money into force modernization programs. The FY 2000 Program Objective Memoranda submitted by the military services to the Office of Secretary of Defense demonstrates that this migration phenomenon is continuing.¹⁹ Consequently, the inability to properly account for funds will continue to add to readiness problems with regard to modernization issues.

QUADRENNIAL DEFENSE REVIEW (QDR)

Mr. Franklin C. Spinney, a noted defense "watchdog", provided the following observations regarding accounting responsibilities during the last Quadrennial Defense Review (QDR).

"The central premise of any representative democracy is that the people can hold representatives accountable. The Framers of our Constitution understood this and designed the system of checks and balances to ensure accountability. One of those checks is that every member of the US government makes a sacred oath to uphold the spirit of the Constitution. Another check is Article 1, Section 9, Clause 7, which requires Congress to publish a "...regular Statement and Account of the Receipts and Expenditures of all public money..." from time to time. The Defense Department's continued toleration of the bookkeeping crisis makes a

mockery of this requirement and therefore violates the spirit, if not the letter, of the Constitution. The cavalier treatment of our oath to support and uphold the Constitution insults the American taxpayers who are being asked to pay the bill, and left unchecked, it undermines our form of government."²⁰

The impact of accounting on assessing military readiness was never more apparent than the financial issues pertaining to the 1997 QDR. Each year, DOD produces a six-year budget plan known as the Future Years Defense Program or FYDP. Although the QDR confidently boasted of military-technical revolutions on electronic battlefields in 2010, the financial analyses indicated that it was difficult to predict what a weapon will cost in three to five years.²¹ Weapons cost projections in the outyears of one FYDP cannot be adequately measured with those in other FYDPs. Consequently, the inability of the QDR to obtain historical and accurate financial costs restricted a full analysis of cost saving measures and assessment of how to properly forecast costs associated with major weapon systems and defense structures. An improved accounting system will eliminate these deficiencies and allow future QDRs to analyze past FYDPs and compare them with current and future FYDPs.

BASE REALIGNMENT AND CLOSURE (BRAC)

Currently, no accounting system exists to track BRAC savings. In the past, military BRAC savings estimates were inconsistently developed and poorly documented.²² The absence of efforts to track or update projected savings indicates the need for additional guidance and emphasis from DOD on accumulating and documenting current savings on a comprehensive and perpetual basis.²³

Closing unneeded and excess defense facilities has historically been difficult because of public concern about the economic effects of closures on small military dependent communities and the perceived partiality of the decision-making process. However, legislation enacted in 1988 (Public law 100-526) supported a special commission chartered by the Secretary of Defense to identify bases for realignment and closure. With this legislation, a BRAC round was completed in 1988. Congress later passed the Defense Base Closure and Realignment Act of 1990 that created an independent commission and authorized three BRAC rounds in 1991, 1993, and 1995. The four BRAC rounds resulted in the closure of 97 of 495 major domestic installations. Many smaller ones were realigned into other facilities.²⁴ A sound methodology for estimating saving estimates is important because DOD relies on these savings for procuring or maintaining defense programs.

LOGISTICS READINESS

For many field commanders, the logistics system is a significant driver of the costs for training and equipping soldiers. Unfortunately, stovepipe and non-interoperable logistics and financial systems hamper the commander's ability to oversee all resource areas to maximize readiness. Every transaction in this system (and any other system) has tremendous impact on the commander's financial resources.²⁵

In August 2000, *The Army Times* published an article concerning the loss of \$900 million in military gear.²⁶ This article is an example of the effect of DOD's nonintegrated systems on the inventory management area. Mr. Ernest Gregory, Deputy Assistant Secretary of the Army (Financial Operations), clarified the problem as the cost differences with inventory valuation, not the physical loss of logistical assets.²⁷ In fact, Mr. Gregory emphasized that DOD has one of the best inventory accountability systems in the world because US commanders are required by regulations to conduct 10% of their full property and equipment inventories each month. However, auditors have repeatedly noted and reported that the lack of integration between DOD's accounting and logistics system contribute significantly to the purchase of unneeded materials.

The DOD is taking aggressive action to improve how it accounts for the value of its inventory. Enhancing logistical and inventory management systems to capture proper accounting information will provide for automated inventory valuation, reliable costing of goods sold, and other elements that enhance accurate operating costs.²⁸

The following example, included in the Army's Chief Financial Officer's Plan, provides an excellent depiction regarding the relationship between logistics and accounting:

A POL clerk of an armor battalion seeks to restock his oil supply with 50 cases of a particular type of oil. In doing so, he enters an erroneous National Stock Number (NSN). The NSN entered has a unit of issue of "drum" rather than "case"—a much more expensive item. Thus, the POL clerk has inadvertently consumed a great deal more of the Commander's resources than planned. In other words, the checkbook balance is lower than expected. In the past, there was more time to discover errors, correct them, and avoid erroneous charges, thereby conserving the unit's funds. That time is being significantly reduced by distribution-based logistics. Order ship times have dropped from 74 days to 34 days in Europe, from 34 to 18 days in Korea; and from 23 days to nine days at Fort Hood. In our example, the check would be cashed more quickly. With an integrated transaction-driven system, the same transaction

that would trigger the supply system would also trigger an immediate entry in the financial management system. The unusually large expenditure from POL would show up immediately on a financial report, providing an accurate checkbook balance. This would increase the likelihood that someone, either a logistician or financial manager, would identify the discrepancy and take corrective action before the unit was charged, thereby conserving scarce resources.

In another scenario, that same unit might have a PLL clerk who is turning in excess parts for which the unit receives a financial credit. Without integrated logistics and financial management processes and systems, the commander is not immediately aware of the additional resources at his disposal. In other words, the deposit would not be entered in his checkbook for several days or weeks.

In a time of constrained budgets, commanders need real-time information about the resources they have available. The increased speed and efficiency in which the logistical system operates demands that it be integrated with the financial management system. Only in this way will the financial management system be able to tell the commander what is really available to train, equip, and care for his unit.²⁹

Timely, accurate and useful information for the commander requires interoperability of logistics and financial systems. In order to prepare, obtain and use financial statements, the financial informational systems must be integrated with, the logistics system, but also with the personnel system, the real property system, and a network of other systems.

SUPPLEMENTAL CONGRESSIONAL APPROPRIATIONS

Although there are significant weaknesses within our current accounting systems, there are areas where accounting already serves a valuable purpose. Accounting currently allows the DOD to track costs during contingency operations. Since 1992, the U.S. Armed Forces have deployed thirty three times³⁰. Participation of the military in these contingency operations costs millions of dollars. In most cases, units participating in these operations must use their own Operations and Maintenance (O&M) funds to deploy and provide support in the areas of operation. By accurately documenting deployment costs, DOD can request supplemental funds from Congress. These supplemental funds are restored to O&M accounts to ensure the force remains manned, equipped and trained.

The use of Accounting Processing Codes (APCs) on procurement and contracting documents has enabled DOD to request and receive critical supplemental appropriations from Congress, thus restoring readiness-related funds to O&M accounts. The meticulous tracking of

flying hours, tank miles driven, logistic supplies and other costs amount to billions of dollars and ensure that DOD can support requests for annual supplemental appropriations.

FINANCIAL REFORMS

With the exception of accounting for supplemental appropriations, this paper has primarily concentrated on the inherent weaknesses of the current accounting system. However, significant reforms are underway to improve and resolve these weaknesses.

CHIEF FINANCIAL OFFICERS ACT (CFO)

The CFO Act of 1990 requires the federal government to produce accurate and auditable financial statements that reflect the actual value of Property, Plant, and Equipment (PP&E) Capital Assets. Its key purpose is to design and implement a better accounting system that provides more timely, accurate, and reliable financial information for decision makers.³¹

The CFO Act ensures significant improvements and enhancements to general and financial management practices in the federal government by requiring the development of an integrated financial management system, including financial reporting and internal controls. The Act also ensures a financial management leadership structure, preparation and audit of financial statements that conform to Generally Accepted Accounting Principles (GAAP), and reinforce accountability reporting.³²

The CFO Act also charges DOD Chief Financial Officers with:

- directing, managing, and providing policy guidance and oversight of all agency financial management personnel, operations and activities.
- developing and maintaining integrated accounting and financial management systems.
- implementing asset management systems, to include cash management.
- monitoring financial execution of the military's budget in relation to actual expenditures.
- overseeing the selection, recruitment, and training of qualified personnel to execute the military's financial management functions.³³

To ensure compliance, the law directed establishment of the Defense Finance and Accounting Service (DFAS) and new financial informational systems to consolidate finance offices and streamline accounting operations. Applying these reforms will aid the DOD in achieving a greater financial return on its financial investments. The following sections provide

information regarding the DFAS role and creation of new information systems to conform with the CFO Act.

DFAS

In 1991, the DFAS was activated to consolidate the numerous Finance & Accounting Offices throughout the military services and reduce the number of financial systems used to track and report accounting data. As the largest finance and accounting firm in the world, the DFAS processes a monthly average of 10 million payments to DOD personnel; 1.2 million commercial invoices; 600,000 travel vouchers/settlements; 500,000 saving bond issuances; and 122,000 transportation bills of lading, with monthly disbursements averaging \$24 billion.³⁴ Given the significance and magnitude of these financial transactions, even the smallest percentage of errors can result in large financial variances and problems.

The DFAS inherited numerous problems and challenges the Military Services had been dealing with since the formation of the Continental Army. To resolve these long-standing problems, financial operations have been consolidated and a significant number of redundant finance and accounting offices reduced and/or closed. As a result, over 330 financial management field sites throughout the world were consolidated into five DFAS Centers and twenty Operating Locations, saving approximately \$120 million annually. These consolidations have enabled the Department of Defense to:

- eliminate redundancy and unnecessary bureaucracy.
- promote standardization; improve the accuracy, and timeliness of our financial operations.
- enhance customer service and support increased productivity.
- provide better financial information and support to the Department's decision makers.³⁵

To resolve numerous outdated and non-compliant accounting systems, the DFAS designed and fielded a number of new standard inventory and accounting systems. As of October 1998, 109 finance and accounting systems were operating – a reduction of 215 systems or 66%. Accounting systems have been reduced from 127 to 18 with a goal of having only 9 by 2003.³⁶

DEFENSE JOINT ACCOUNTING SYSTEM (DJAS)

In 1996, the Under Secretary of Defense (Comptroller) directed the acquisition of a new transaction-driven general accounting system to replace the current Standard Financial System (STANFINS). STANFINS does not comply with generally accepted accounting principles and federal guidelines. The Defense Joint Accounting System (DJAS) is part of the DFAS migration strategy for general and business fund accounting systems as outlined in the DFAS Accounting Systems Strategic Plan, which was released in 1997. When completed, DJAS will provide a financial accounting system to support the Joint Services and Defense Agencies.³⁷ DJAS provides information superiority by increasing access to financial and accounting information. The major functions provided by DJAS include general ledger, accounts receivable, funds control, accounts payable, financial reports, cost management and core financial systems.³⁸

DEFENSE PROPERTY ACCOUNTABILITY SYSTEMS (DPAS)

The DOD identified real property accounting as a high-risk area in FY 1990. The Federal Managers' Financial Integrity Act (FMFIA) Annual Statement of Assurance for FY 1993 reported financial accounting for real property as one of the five high-risk areas within the Military Department. Financial property accountability requirements and ongoing corrective actions are documented within the DOD Chief Financial Management Officer's 5-Year Plan dated October 1995.³⁹

The Defense Property Accountability System (DPAS) is the DOD's real property accountability system identified to repair the Department's weaknesses identified in the FMFIA and CFO Acts. DPAS currently complies with DOD Financial Management Regulations (FMR) by providing asset accountability, general ledger accounting, cost improvement visibility, capital asset reports and financial system interfaces with nine standard accounting transactions. The objectives of DPAS are as follows:

- Provide physical and financial control over property
- Ensure integration of financial and property data
- Enforce regulatory financial and physical reporting of property, FMR and CFO Compliance
- Eliminate redundant systems and costs

- Provide system interfaces to DOD migratory accounting systems
- Become the single point of data entry
- Provide asset visibility and redistribution
- Ensure technical migration

The DPAS will ensure that all property, plant, and equipment with an initial acquisition cost (above the Department's threshold effective at the time of acquisition and a useful life of 2 years or greater) is brought under general ledger control and reported in their entirety in financial statements. In addition, summary property records will be reconciled to departmental-level account balances to ensure clear and accurate audit trails.

ACCOUNTING AND ACTIVITY-BASED COSTING (ABC)

Tracking installation and project overhead costs is a major objective for most Major Command and garrison installations. Commanders and managers are using a new accounting concept entitled Activity-Based Costing to more closely track these costs. To better understand this concept, two definitions of Activity Based Accounting are provided: Activity Based Costing (ABC) and Activity Based Management.

ABC is a two-stage cost allocation process. The first stage identifies the overhead or activity being tracked and the second stage assign cost objects within that particular activity. For example, in a vehicle maintenance shop, the shop is considered the activity and cost objects would include such items as the number of maintenance requests, inventory movements, and purchase order requests.

By definition, ABC is a "method of measuring the cost and performance of activities and cost objects. Under ABC, costs are assigned to activities based on their use of resources and assigns costs to cost objects based on their use of activities. ABC recognizes the causal relationship of cost drivers to activities."⁴⁰ The primary focus of ABC is to break out indirect activities into meaningful groups that can then be assigned to management processes, which better reflect the way costs are actually incurred. Simply stated, ABC is nothing more than separating a major cost element from the overhead pool and assigning it to cost objects based on some less arbitrary means than direct labor. ABC can assist in tracking costs by addressing the following issues:

- Improving pricing and credit strategies
- Understanding the level of required inventory to support requirements
- Enhancing predictive ability for the cost of future equipment and supplies

- Identifying and tracking the cost of other types of cost objects
- Attaching below the line costs to the original product cost model
- Identifying process dysfunction and improvement.⁴¹

Activity Based Management is a process that focuses on the management of activities as the route to continuously improve the value received by its customers and the benefits achieved by providing this value.⁴² The discipline included with Activity Based Management provides cost driver analysis, activity analysis, and performance analysis.

The use of an Activity Based Costing and Management model within the military will lead to enhancing the department's ability to identify and track costs. Specifically, the activity-based model ties together the financial system and the various operational systems of the organization. These improvements can take the form of incremental process improvements using Total Quality, Just-In-Time or Reengineering Management. In the end, Activity Based Costing and Management will measure the relative success of the changes implemented and aid in operational decisions leading to better utilization of financial resources within organizations.

CONCLUSIONS

Through GAO and Defense Audit Agencies, DOD has recognized the need to resolve accounting weaknesses and improve the interoperability of its financial systems. A DOD Financial Management Plan was developed as the 'blueprint' to meet the challenges of its six most significant problem areas. The problem areas include: integrating accounting and financial management systems; accumulating accurate cost information; resolving problem disbursements; upgrading financial management workforce and organization; improving financial control procedures; and reengineering business practices. Once these problems are resolved, improved accounting systems will significantly assist the military decision maker by providing timely financial data and analyses. DOD financial managers must understand the implications of reliable and accurate financial information on their overall accountability and effective management of critical mission operations.

Tracking military expenditures and disbursements in an accurate and reliable manner will enhance accountability of public funds and ensure DOD's credibility to the American People. Following mandated congressional legislation, including the CFO Act and the establishment of the Defense Finance and Accounting Service, the DOD is moving steadily to increase the accuracy, reliability and timeliness of financial information. Government compliant and

interoperable financial systems such as the Defense Property Accounting System and Defense Joint Accounting Systems will ensure that financial data meets the legalities of the CFO Act.

RECOMMENDATIONS

The following recommendations are submitted to improve the accounting system and assist the military decision-maker. DOD must:

- continue to develop and improve upon its 5-year Financial Management Plan.
- create or modify its accounting system to track BRAC savings.
- integrate accounting into the business reengineering process and provide value-added analysis.
- incorporate Activity Based Costing as a primary tool to identify costs at installation levels.
- educate and train military leaders on the importance and use of accounting reports and analyses.

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ENDNOTES

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