

**Audit**



**Report**

OFFICE OF THE INSPECTOR GENERAL

CONSISTENCY IN REPORTING THE  
EXPENSE ACCOUNT LINE ITEMS OF THE  
DEFENSE BUSINESS OPERATIONS FUND

Report No. 97-062

January 7, 1997

Department of Defense

### **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, VA 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](mailto:Hotline@DODIG.OSD.MIL); or by writing the Defense Hotline, The Pentagon, Washington, D.C. 20301-1900. The identity of each writer and caller is fully protected.

### **Acronyms**

DBOF	Defense Business Operations Fund
DeCA	Defense Commissary Agency
DFAS	Defense Finance and Accounting Service
DLA	Defense Logistics Agency
GLAC	General Ledger Account Code
OMB	Office of Management and Budget



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



January 7, 1997

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

**SUBJECT: Audit Report on Consistency in Reporting the Expense Account Line Items of the Defense Business Operations Fund (Report No. 97-062)**

We are providing this audit report for review and comments. It is the first in a series of reports to be issued as a result of the Audit of Expense Accounts in the FY 1996 Financial Statements of the Defense Business Operations Fund.

Management comments on a draft of this report were generally responsive and were considered in preparing the final report. DoD Directive 7650.3 requires that all recommendations be resolved promptly. We request that the Under Secretary of Defense (Comptroller) reconsider his position on Recommendation 1.a. and provide additional comments to this final report by March 7, 1997. Comments should also include the completion date for revising DoD 7000.14-R, volume 11B.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Richard B. Bird, Audit Program Director, at (703) 604-9145 (DSN 664-9145), or Mr. Carmelo G. Ventimiglia, Audit Project Manager, at (317) 542-3852 (DSN 699-3852). The distribution of this report is in Appendix E. The audit team members are listed inside the back cover.

A handwritten signature in black ink that reads "Robert J. Lieberman".

Robert J. Lieberman  
Assistant Inspector General  
for Auditing

## Office of the Inspector General, DoD

Report No. 97-062  
(Project No. 5FI-2016)

January 7, 1997

### Consistency in Reporting the Expense Account Line Items of the Defense Business Operations Fund

#### Executive Summary

**Introduction.** The Chief Financial Officers Act of 1990, as amended, requires an annual audit of the financial statements of the Defense Business Operations Fund. The Statement of Operations (and Changes in Net Position) (referred to as the Statement of Operations) is one of the Defense Business Operations Fund financial statements. The Statement of Operations for individual reporting entities must be prepared with consistency to ensure that balances are presented uniformly and accurately on the consolidated statements. The issue of consistency in reporting the \$80.1 billion in expense account line items was identified during the Audit of Expense Accounts in the FY 1996 Financial Statements of the Defense Business Operations Fund. This report will be the first in a series of reports on the area.

**Audit Objectives.** The overall audit objective was to determine whether the expenses on the FY 1996 Consolidated Financial Statements of the Defense Business Operations Fund were presented fairly in accordance with the other comprehensive basis of accounting described in Office of Management and Budget Bulletin No. 94-01, "Form and Content of Agency Financial Statements," November 16, 1993, or subsequent issuances. As part of that objective, we evaluated how the Defense Finance and Accounting Service Centers calculated and presented expense account line items on the FY 1995 Statements of Operations they prepared for reporting entities.

**Audit Results.** The Defense Finance and Accounting Service Centers did not consistently calculate and present expense account line items for the Defense Business Operations Fund on the FY 1995 Statements of Operations they prepared for reporting entities in the Supply Management business area. As a result, of the \$80.1 billion of expense account line items on the individual Statements of Operations, at least \$1.6 billion of the \$47 billion we reviewed was misclassified, thus preventing an accurate consolidation of Defense Business Operations Fund financial information.

**Summary of Recommendations.** We recommend that the Under Secretary of Defense (Comptroller) revise DoD 7000.14-R, "Financial Management Regulation," volume 11B, "Reimbursable Operations, Policy and Procedures--Defense Business Operations Fund," and update "DoD Guidance on Form and Content of Financial Statements for FY 1994/1995 Financial Activity" to correct inconsistencies with the guidance in Office and Management Budget Bulletin No. 94-01, "Form and Content of Agency Financial Statements." We also recommend that the Under Secretary of Defense (Comptroller) require all operating expenses of the Defense Commissary Agency be presented on line 9, Program or Operating Expenses, on the Statement of Operations. We recommend that the Director, Defense Finance and Accounting Service, review the methodologies used by the reporting entities and Defense Finance and Accounting Service Centers in calculating and presenting expense account line items on the Statements of Operations to ensure compliance with prescribed guidance.

**Management Comments.** The Deputy Chief Financial Officer, Office of the Under Secretary of Defense (Comptroller), consolidated comments from the Defense Finance and Accounting Service with his response. His office and the Defense Finance and Accounting Service agreed with our finding and recommendations except for the recommendation to categorize cost of goods sold as either "To the Public" or "Intragovernmental." The Deputy Chief Financial Officer stated that the cost of goods sold does not differ based upon the customer and by categorizing cost of goods sold as either public or intragovernmental, users of the Defense Business Operations Fund financial statements could be misled. He further stated that such an accounting treatment would create a compliance cost, without benefit, and add to the complexity of accounting and cost allocation. A discussion of the management comments is in Part I and the complete text is in Part III.

**Audit Response.** We consider the comments of the Deputy Chief Financial Officer to be partially responsive. While the actual cost of the goods sold would be the same regardless of whether the customer is another governmental unit or the public, differentiating between the cost that relates to sales made to the public and sales made to other governmental units is important. Defense Business Operations Fund managers eventually may make business decisions based on that information. However, at this time, the main benefit of categorizing the cost of goods sold would be to help identify abnormal situations that should be researched and corrected before the financial statements are issued. Office of Management and Budget Bulletin No. 94-01 and "DoD Guidance on Form and Content of Financial Statements for FY 1994/1995 Financial Activity" require that cost of goods sold be presented on the financial statements as either "To the Public" or "Intragovernmental." Abnormal situations may indicate problems with how revenue and expense transactions are classified. We also recognize that the form and content of the financial statements will change in FY 1998. In the meantime, Defense Finance and Accounting Service Center personnel should identify and correct abnormal relationships between revenue and cost related to sales made to the public and sales made to other governmental units. Including a breakdown of cost of goods sold in the monthly Accounting Reports 1307 would help to identify abnormal situations. Defense Finance and Accounting Service Center personnel stated that the information is available to categorize cost of goods sold on the Accounting Reports 1307. In addition, although the Deputy Chief Financial Officer concurred with the recommendation to update DoD 7000.14-R, volume 11B, he did not provide the planned completion date.

We request that the Under Secretary of Defense (Comptroller) reconsider his position and provide additional comments to this final report, including the completion date for revising DoD 7000.14-R, volume 11B, by March 7, 1997.

# Table of Contents

---

<b>Executive Summary</b>	<b>i</b>
<b>Part I - Audit Results</b>	
Audit Background	2
Audit Objectives	3
Presentation of Financial Data	4
<b>Part II - Additional Information</b>	
Appendix A. Scope and Methodology	14
Scope	14
Methodology	15
Appendix B. Summary of Prior Audits and Other Reviews	17
Appendix C. Major Expense Account Line Items and General Ledger Accounts	19
Appendix D. Organizations Visited or Contacted	21
Appendix E. Report Distribution	22
<b>Part III - Management Comments</b>	
Under Secretary of Defense (Comptroller) Comments	26

## **Part I - Audit Results**

## Audit Background

The Audit of Expense Accounts in the FY 1996 Financial Statements of the Defense Business Operations Fund (DBOF) is part of the overall Audit of the FY 1996 Consolidated Financial Statements of the DBOF. The Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994 (Public Law 103-356, October 13, 1994), requires annual audits of funds such as the DBOF. The Federal Financial Management Act of 1994 also requires that Government-wide financial statements be prepared annually beginning in FY 1997.

The Federal Accounting Standards Advisory Board was established to recommend Federal accounting standards to the Director, Office of Management and Budget (OMB); the Secretary of the Treasury; and the Comptroller General, who are the principals of the Joint Financial Management Improvement Program. Accounting standards for the Federal Government remain under development. Until all aspects of financial statement reporting are governed by accounting standards that will constitute "generally accepted accounting principles for the Federal Government," agencies are required to follow the hierarchy described in OMB Bulletin No. 94-01, "Form and Content of Agency Financial Statements," November 16, 1993. A summary of the hierarchy is as follows:

- o standards agreed to and published by the Joint Financial Management Improvement Program Principals,
- o form and content requirements of the OMB,
- o accounting standards in agency guidance on accounting policies, and
- o accounting principles published by other authoritative sources.

"DoD Guidance on Form and Content of Financial Statements for FY 1994/1995 Financial Activity," (DoD Guidance on Form and Content) as amended on November 27, 1995, has guidance for preparing DoD financial statements. DoD 7000.14-R, "Financial Management Regulation," volume 11B, "Reimbursable Operations, Policy and Procedures--Defense Business Operations Fund," December 1994, (volume 11B of the Financial Management Regulation) provides the policies and procedures for reimbursable operations, including guidance on preparing the DBOF Accounting Report 1307 (Accounting Report 1307). The Accounting Report 1307 provides management with a monthly report on DBOF operations.

The DBOF was established in October 1991 by merging into a single fund the former stock and industrial funds and several organizations previously funded with direct appropriations. The purpose of the DBOF is to improve delivery of support services to DoD operating forces while reducing the cost of operations. The providers in the DBOF customer-provider relationship are the business

areas, each of which is under the management control of a designated DoD component. The DBOF has 13 business areas, the largest of which is the Supply Management business area. All of the Statements of Operations (and Changes in Net Position) (referred to as the Statement of Operations) for the DBOF reporting entities are combined to prepare the consolidated DBOF Statement of Operations. The Defense Finance and Accounting Service (DFAS) reported about \$80.1 billion in DBOF expenses on the FY 1995 consolidated Statement of Operations. Information in the individual financial statements is the joint responsibility of the DBOF reporting entity and the DFAS Center responsible for preparing the financial statements.

## **Audit Objectives**

The overall audit objective was to determine whether the expenses on the FY 1996 Consolidated Financial Statements of the DBOF were presented fairly in accordance with the other comprehensive basis of accounting described in OMB Bulletin No. 94-01, or subsequent issuances. As part of that objective, we evaluated how the DFAS Centers calculated and presented expense account line items on the FY 1995 Statements of Operations they prepared for reporting entities. See Appendix A for a discussion of the audit scope and methodology. See Appendix B for a summary of prior audit coverage related to the audit objectives.

---

## Presentation of Financial Data

The DFAS Centers did not consistently calculate and present expense account line items in the individual FY 1995 Statements of Operations they prepared for DBOF reporting entities in the Supply Management business area. The lack of uniformity in reporting occurred because of conflicting guidance among OMB Bulletin No. 94-01, DoD Guidance on Form and Content, and volume 11B of the Financial Management Regulation, and personnel at the DFAS Centers not following prescribed procedures. In addition, personnel in the Office of the Under Secretary of Defense (Comptroller) and Headquarters, DFAS, did not effectively monitor the reporting of expenses on the individual Statements of Operations. As a result, of the \$80.1 billion of expense account line items on the individual Statements of Operations, at least \$1.6 billion of the \$47 billion we reviewed were misclassified, thus preventing an accurate consolidation of DBOF financial information.

## Guidance for Presenting Expense Account Line Items

**Office of Management and Budget Bulletin No. 94-01.** OMB Bulletin No. 94-01 directs each executive agency to prepare financial statements and submit them to the Director of the OMB. The bulletin also identifies the form and content to be included in the financial statements.

**DoD Guidance for Preparing Financial Statements.** The Chief Financial Officer of the DoD, the Under Secretary of Defense (Comptroller), issues guidance for implementing OMB policies. DoD Guidance on Form and Content assigns responsibilities for preparing and submitting the financial statements required by the Chief Financial Officers Act. The DBOF consists of multiple divisions identified by DoD component and business area. DoD components are responsible for the accuracy of the information entered into financial systems or provided to DFAS for reporting in financial statements. DFAS is responsible for maintaining the integrity of the financial information provided by each reporting entity and for preparing the financial statements. The Supply Management business area involves the inventory management of supplies and repair parts that are sold to a wide variety of DBOF customers. The Supply Management DBOF business area accounts for more expenses than any other business area.

**Volume 11B of the Financial Management Regulation.** Volume 11B of the Financial Management Regulation requires the Director, DFAS, to establish procedures to ensure that DBOF policies are implemented and to evaluate the operation of DBOF organizations to ensure compliance with established requirements. Volume 11B of the Financial Management Regulation also contains guidance for preparing the Accounting Report 1307. One of the principal statements required by the Chief Financial Officers Act, and included as part of Accounting Report 1307, is the Statement of Operations.

The Statement of Operations discloses the results of the reporting entity's operations for the reporting period, including changes in the entity's net position from the end of the prior reporting period. The Accounting Report 1307 provides DBOF managers with an important tool to track monthly performance. The Statement of Operations identifies six expense account line items. About \$79.3 billion (99 percent) of the \$80.1 billion in expenses in the FY 1995 Consolidated Statement of Operations was reported on line 9, Program or Operating Expenses; line 10, Cost of Goods Sold; and line 14, Other Expenses. Appendix C defines the three expense account line items and the major standard general accounts that are to be used in calculating each line item.

## Reporting Program or Operating Expenses

**Clarifying Existing Guidance.** The guidance for reporting program or operating expenses in volume 11B of the Financial Management Regulation sometimes was in conflict with OMB Bulletin No. 94-01 and DoD Guidance on Form and Content. In addition, guidance on reporting the Operations area of the Defense Commissary Agency (DeCA) was not correct. Consequently, personnel at the DFAS Centers misclassified some DBOF expenses.

**General Ledger Account Code 6900, Other Expenses.** The DFAS Centers inconsistently reported the financial data in general ledger account code (GLAC) 6900, Other Expenses, on Statement of Operations because the procedures in volume 11B of the Financial Management Regulation did not conform to the guidance in OMB Bulletin No. 94-01 and DoD Guidance on Form and Content. OMB guidance and DoD Guidance on Form and Content appropriately required that GLAC 6900 be included in calculating line 14, Other Expenses. However, volume 11B of the Financial Management Regulation required that GLAC 6900 be used instead to calculate line 9, Program or Operating Expenses. We reviewed the methodologies used by the DFAS Cleveland Center, Cleveland, Ohio; DFAS Columbus Center, Columbus, Ohio; DFAS Denver Center, Denver, CO; DFAS Indianapolis Center, Indianapolis, IN; and DFAS Kansas City Center, Kansas City, MO, (the DFAS Centers) to prepare the Statement of Operations for each DBOF reporting entity. We found that personnel at the DFAS Cleveland Center, DFAS Columbus Center, and DFAS Kansas City Center incorrectly included \$547.7 million for GLAC 6900 on line 9, Program or Operating Expenses, and line 10, Cost of Goods Sold. A similar conflict in guidance existed for GLAC 6330, Interest. To ensure that the DBOF financial statements will be consistent with other DoD financial statements, the guidance in volume 11B of the Financial Management Regulation should be revised to be consistent with the guidance in OMB Bulletin No. 94-01 and DoD Guidance on Form and Content.

**Reporting DeCA Operating Expenses.** DoD Guidance on Form and Content and volume 11B of the Financial Management Regulation inappropriately required that the operating expenses in the Operations area of DeCA be reported on line 10, Cost of Goods Sold. DoD Guidance on Form

## Presentation of Financial Data

---

and Content and volume 11B of the Financial Management Regulation required that operating expenses be presented as a cost of services sold, except in the Supply Management business area and the DeCA Resale area where operating expenses were to be reported on line 9, Program or Operating Expenses. The operating expenses of the DeCA Operations area are those costs incurred in conducting the normal operations of the DeCA Resale area, a Supply Management business area. Because the DeCA Operations area does not manufacture or sell any product, the operating expenses of the DeCA Operations area should be reported on line 9, Program or Operating Expenses. DFAS Columbus Center personnel followed the guidance in DoD Guidance on Form and Content and volume 11B of the Financial Management Regulation by reporting the \$1.1 billion of operating expenses of the DeCA Operations area for FY 1995 on line 10, Cost of Goods Sold, instead of on line 9, Program or Operating Expenses. Consequently, on the DeCA FY 1995 Statement of Operations, line 9, Program or Operating Expenses, was misclassified by the \$1.1 billion incorrectly reported on line 10, Cost of Goods Sold.

## Cost of Goods Sold

The DFAS Centers did not correctly calculate line 10, Cost of Goods Sold. Some differences existed between DoD Guidance on Form and Content and volume 11B of the Financial Management Regulation, and personnel at the DFAS Centers had not established and used the standard general ledger accounts necessary to properly compute cost of goods sold. Further, the methodologies used by personnel at the DFAS Centers to compute expense account line items on the FY 1995 Statement of Operations often varied from those used to prepare the year-end Accounting Report 1307.

**Guidance on Calculating Cost of Goods Sold.** Policies and procedures in DoD Guidance on Form and Content and volume 11B of the Financial Management Regulation for computing the cost of goods sold were essentially the same. The major differences were as follows.

- o Volume 11B of the Financial Management Regulation requires the use of GLAC 1529.1E, Material Returns - Credit Given, and GLAC 1529.3, Allowance for Repairs, in computing the cost of goods sold on the Statement of Operations, whereas DoD Guidance on Form and Content includes GLACs 1529.1E and 1529.3 in computing line 14, Other Expenses. The balances in those general ledger accounts should be added to the value of the beginning inventory because the material and depot level repairable items were added to inventory during the period and should be counted as sold if they are not included in ending inventory.

- o Volume 11B of the Financial Management Regulation requires the use of the Inventory Losses Realized account, the net of inventory gains and inventory losses, in computing line 14, Other Expenses, whereas DoD Guidance on Form and Content includes inventory gains in line 10, Cost of Goods Sold, but transfers inventory losses to line 14, Other Expenses. By following the

guidance in DoD Form and Content, line 14, Other Expenses, would show a higher dollar amount on the financial statements than on the Accounting Reports 1307.

**Computation Varies Among DFAS Centers.** The DFAS Centers did not properly establish and use the Allowance for Unrealized Holding Gains and Losses account in computing the cost of goods sold. Each DFAS Center used the financial data provided by the reporting entities in computing the cost of goods sold. However, significant differences existed in how the data were used and adjusted by each of the DFAS Centers. For example, Army DBOF organizations crosswalked financial data into GLAC 6500, Cost of Goods Sold. DFAS Indianapolis Center personnel subsequently adjusted GLAC 6500, Cost of Goods Sold, to agree with line 10, Cost of Goods Sold, on the Accounting Report 1307 prepared as of September 30, 1995. DFAS Indianapolis Center personnel did not calculate cost of goods sold in accordance with volume 11B of the Financial Management Regulation because they did not map general ledger accounts to the computation lines. The DFAS Denver Center used a six-step manual calculation process that did not agree with either volume 11B of the Financial Management Regulation or DoD Guidance on Form and Content. Because of the differences in how the DFAS Centers calculated the cost of goods sold on the individual Statements of Operations, line 10, Cost of Goods Sold, was not comparable for the reporting entities in the Supply Management business area.

**Usefulness of Reported Data.** The usefulness of the Accounting Report 1307 could be further enhanced if line 10, Cost of Goods Sold, was broken down the same way as shown on the Statement of Operations. The Statement of Operations differentiates between the costs that relate to sales made to the public and sales made to other governmental units. To maintain consistency between the two financial reports and provide DBOF managers with additional management information on a monthly basis, the Under Secretary of Defense (Comptroller) should revise volume 11B of the Financial Management Regulation to ensure that revenues and the cost of goods sold differentiate between "To the Public" and "Intragovernmental" on the Accounting Report 1307. Otherwise, abnormal situations may not be identified and researched before financial statements are issued. For example, the DeCA Operations Area reported \$24.8 million in revenues from sales to the public in its FY 1995 Statement of Operations, but did not report any related cost of goods sold.

## Other Expenses

**Procedures for Calculating Line 14, Other Expenses.** The DFAS Centers did not use the same financial data to calculate line 14, Other Expenses, in the individual Statements of Operations. Personnel responsible for preparing the financial statements at the DFAS Centers indicated they were not clear as to what data should be used to report line 14, Other Expenses. The main problem was that the guidance in volume 11B of the Financial Management Regulation

## Presentation of Financial Data

---

differed from the guidance in OMB Bulletin No. 94-01 and DoD Guidance on Form and Content. Both OMB Bulletin No. 94-01 and DoD Guidance on Form and Content indicated that line 14, Other Expenses, should be computed using data in GLAC 6900, Other Expenses; GLAC 7210, Losses on Disposition of Assets; GLAC 7290, Other Losses; and GLAC 7600, Change in Actuarial Liability. In contrast, volume 11B of the Financial Management Regulation indicated that the same line item should be computed using data in GLAC 7210, Losses on Disposition of Assets; GLAC 7291, Inventory Losses and Adjustments; and GLAC 7293, Other Miscellaneous Losses. The Army Audit Agency reported that DFAS Indianapolis Center personnel did not use GLAC 7290, Other Losses, in calculating line 14, Other Expenses. As a result, line 14, Other Expenses, was understated by \$2.2 billion. Subsequently, DFAS Indianapolis Center personnel took actions to correct the expenses reported on line 14, Other Expenses.

Significant differences existed in how line 14, Other Expenses, was calculated and presented in the financial statements and Accounting Reports 1307 as of September 30, 1995. The following table compares the dollar values of expenses reported on line 14, Other Expenses, of the FY 1995 financial statements with the Accounting Reports 1307.

Comparison of Expenses Reported on Line 14, Other Expenses (millions)		
Reporting Entity	Financial Statement	Accounting Report 1307
Army	\$2,462	\$ 104
Navy	191	3,789
Air Force	3,704	0
DoD Agencies	1,727	1,726
Total	\$8,084	\$5,619

The Director, DFAS, should ensure that all appropriate expenses are included in line 14, Other Expenses, on both the financial statements and the Accounting Reports 1307.

## Management Oversight

Personnel in the Office of the Under Secretary of Defense (Comptroller) and Headquarters, DFAS, had not appropriately monitored how the DFAS Centers used data provided by reporting entities in calculating and presenting the expense account line items on the Statement of Operations. Financial statements, including the Statement of Operations, have been prepared for the

DBOF since FY 1992. However, prior to FY 1995, the role of higher headquarters personnel in monitoring the presentation of expense account line items on the Statement of Operations was limited. Furthermore, the Inspector General, DoD, and the Service audit organizations had focused their audit efforts on the DBOF Statement of Financial Position. In FY 1995, the Inspector General, DoD, and the Service audit organizations began to perform audits of the DBOF Statement of Operations. Personnel in the Office of the Under Secretary of Defense (Comptroller) and Headquarters, DFAS, also intensified their reviews of how expense account line items were presented on the Statement of Operations. For example, personnel in the Office of the Under Secretary of Defense (Comptroller) were involved in reviewing problems in valuing the Navy DBOF inventory as of September 30, 1995. An action officer from that office developed a model that should be useful in valuing inventory and computing the cost of goods sold. Personnel in the Office of the Under Secretary of Defense (Comptroller) and Headquarters, DFAS, told us that they planned to continue reviewing how the DBOF financial statements are prepared. To ensure consistency in calculating and presenting expense account line items on the financial statements and the Accounting Reports 1307, they should review the methodologies used by the DBOF reporting entities and the DFAS Centers. Special attention should be given to how DBOF reporting entities and the DFAS Centers establish and use the inventory allowance account in computing cost of goods sold.

### Summary

The Statements of Operations that are prepared monthly as part of the Accounting Report 1307 should be in the same form and have the same content as the annual financial statements required by the Chief Financial Officers Act. Differences in guidance that prevent this from happening should be corrected. Personnel in Headquarters, DFAS, along with personnel in the Office of the Under Secretary of Defense (Comptroller) must closely monitor the reporting of DBOF expense data. If the causes for the problems in calculating and presenting DBOF expense account line items are not corrected, the results of operations in future years will not be fairly presented on the DoD-wide and Government-wide financial statements. The Accounting Report 1307 is one of the most important tools that DBOF managers have to track performance throughout the year. Financial data in the Accounting Report 1307 can help DBOF managers identify financial problems and assist them in making adjustments needed to improve operations during the year. Preparing the Accounting Report 1307 in the same format as the financial statements required by the Chief Financial Officers Act should also help to shorten the time required to prepare and issue the financial statements. Resolving conflicts in guidance among OMB Bulletin No. 94-01, DoD Guidance on Form and Content, and volume 11B of the Financial Management Regulation will help to ensure comparability of the financial data on the DBOF Statement of Operations.

## Recommendations, Management Comments, and Audit Response

### 1. We recommend that the Under Secretary of Defense (Comptroller):

a. **Revise DoD 7000.14-R, "Financial Management Regulation" volume 11B, "Reimbursable Operations, Policy and Procedures--Defense Business Operations Fund," to conform with Office of Management and Budget Bulletin No. 94-01, "Form and Content of Agency Financial Statements." Specifically, require the following.**

o **Include standard general ledger account code 6900, Other Expenses, on line 14, Other Expenses, on Defense Business Operations Fund Accounting Report 1307;**

o **Present all the Defense Commissary Agency operating expenses on line 9, Program or Operating Expenses, on the Statement of Operations (and Changes in Net Position);**

o **Categorize cost of goods sold as either "To the Public" and "Intragovernmental" on Defense Business Operations Fund Accounting Report 1307; and**

o **Designate the specific standard general ledger account codes that are to be included on line 14, Other Expenses, on the Statement of Operations (and Changes in Net Position).**

**Management Comments.** The Deputy Chief Financial Officer, Office of the Under Secretary of Defense (Comptroller), partially concurred. He agreed to include all the recommended changes in the revised version of volume 11B except for categorizing cost of goods sold as either "To the Public" or "Intragovernmental." The Deputy Chief Financial Officer stated that the cost of goods and services sold does not differ based upon the customer. Consequently, a financial statement categorization of the cost of goods and services sold as either public or intragovernmental could lead a user of the DBOF financial statements to infer that the cost of a good or service differed based upon the customer when that is not the case. He further stated that such an accounting treatment would create a compliance cost, without benefit, and add to the complexity of accounting cost allocation.

**Audit Response.** The comments of the Deputy Chief Financial Officer were partially responsive. While the actual cost of the goods sold and services would be the same regardless of whether the customer is another governmental unit or the public, differentiating between the cost that relates to sales made to the public and sales made to other governmental units is important. DBOF managers eventually may make business decisions based on that information. However, at this time, the main benefit of categorizing the cost of goods sold would be to help identify abnormal situations that should be researched and corrected before the financial statements are issued. OMB Bulletin No. 94-01 and DoD Guidance on Form and Content require that cost of goods sold be

presented on the financial statements as either "To the Public" or "Intragovernmental." Abnormal situations may indicate problems with how revenue and expense transactions are classified.

We also recognize that the form and content of the financial statements will change in FY 1998. In the meantime, DFAS Center personnel should identify and correct abnormal relationships between revenue and cost related to sales made to the public and sales made to other governmental units. Including a breakdown of cost of goods sold in the monthly Accounting Reports 1307 would help to identify abnormal situations. DFAS Center personnel stated that information is available to categorize cost of goods sold on the Accounting Reports 1307. We request that the Under Secretary of Defense (Comptroller) reconsider his position when replying to the final report. In addition, we request that a target date for revising volume 11B be furnished.

**b. Revise DoD Guidance on Form and Content of Financial Statements for FY 1996 Financial Activity to ensure that the guidance for preparing the Defense Business Operations Fund Statement of Operations (and Changes in Net Position) is the same as in DoD 7000.14-R, "Financial Management Regulation" volume 11B, "Reimbursable Operations, Policy and Procedures--Defense Business Operations Fund."**

**Management Comments.** The Deputy Chief Financial Officer concurred and stated that "DoD Guidance on Form and Content of Financial Statements for FY 1996 Financial Activity" was revised in October 1996 to be consistent with the guidance in volume 11B. He also stated that volume 11B is currently under revision and, when revised, may include changes that are currently not in "DoD Guidance on Form and Content of Financial Statements for FY 1996 Financial Activity."

**Audit Response.** The comments of the Deputy Chief Financial Officer were responsive. We recognize the need for changes to volume 11B. However, revisions to volume 11B must be consistent with guidance issued by OMB.

**2. We recommend the Director, Defense Finance and Accounting Service, review the methodologies used by the Defense Business Operations Fund reporting entities and the Defense Finance and Accounting Service Centers to ensure consistency in calculating the expense account line items on the individual Statements of Operations (and Changes in Net Position). Specifically, ensure the establishment and use of the inventory allowance account in computing the cost of goods sold.**

**Management Comments.** The Deputy Chief Financial Officer concurred and stated that in September and October 1996 representatives of Headquarters, DFAS, met with personnel from DeCA and the DFAS Centers to review the methodologies that should be used in reporting allowance amounts and computing the cost of goods sold. He stated that representatives of Headquarters, DFAS, will continue to schedule periodic working sessions with the DFAS Centers and other appropriate offices to ensure financial reports and

## **Presentation of Financial Data**

---

statements are in compliance with the DoD Financial Management Regulations, DoD Guidance on Form and Content of Financial Statements, and other applicable DoD guidance.

**Audit Response.** The comments of the Deputy Chief Financial Officer were responsive. Future meetings should include representatives from DLA.

## **Part II - Additional Information**

## Appendix A. Scope and Methodology

### Scope

As part of the Audit of Expense Accounts in the FY 1996 Financial Statements of the DBOF, we reviewed how expense account line items were computed and presented on the FY 1995 Statements of Operations for DBOF reporting entities. The review included three of the four material expense account line items in the FY 1995 Consolidated Statement of Operations of the DBOF. The three line items we reviewed were line 9, Program or Operating Expenses; line 10, Cost of Goods Sold; and line 14, Other Expenses. The review concentrated on the Supply Management business areas under the control of the Military Services and DLA. We also reviewed the financial reporting of the Resale and Operations areas of DeCA. The three line items accounted for about \$47 billion (59 percent) of the \$80.1 billion in total expenses reported by all entities in the FY 1995 Statement of Operations. Table A-1 summarizes the scope of our review.

Table A-1. Dollar Values, by Category of Reporting Entity, of the Expense Account Line Items in the Statement of Operations (and Changes in Net Position) for Period Ended September 30, 1995 (billions)

Expense Account Line Item	Category of Reporting Entity			
	Supply Management Organizations	Defense Commissary Agency	Non-Supply Management Organizations	All Reporting Entities
Program or Operating Expenses	\$ 5.4	\$ 0.0	\$ 2.4	\$ 7.8
Cost of Goods and Services Sold	26.9	6.6	29.7	63.2
Depreciation and Amortization	0.0	0.0	0.8	0.8
Bad Debts and Writeoffs	0.0	0.0	0.0	0.0
Interest	0.0	0.0	0.0	0.0
Other Expenses	8.1	0.0	0.2	8.3
<b>Total</b>	<b>\$40.4</b>	<b>\$6.6</b>	<b>\$33.1</b>	<b>\$80.1</b>

We limited our review to how the DFAS Centers used the financial data in the standard general ledger accounts. We did not evaluate the transactions that were used to populate the general ledger accounts.

## Methodology

We reviewed and compared guidance for preparing the annual Statement of Operations required by the Chief Financial Officers Act and the monthly DBOF Accounting Reports 1307. We interviewed personnel at the five DFAS Centers to determine how they used the financial data furnished by the reporting entities in preparing the financial statements and the accounting reports. Table A-2 identifies the DFAS Centers that prepared financial statements and accounting reports for reporting entities in the Supply Management business area.

Reporting Entity	DFAS Centers				
	Cleveland	Columbus	Denver	Indianapolis	Kansas City
Army				X	
Navy	X				
Marine Corps					X
Air Force			X		
DLA		X			
DeCA		X			

We also reviewed the process used by DFAS Indianapolis Center personnel for consolidating the information from the individual financial statements into the consolidated DBOF financial statements. Further, we discussed the presentation of expense account line items on the Statement of Operations with personnel from the Office of the Under Secretary of Defense (Comptroller) and Headquarters, DFAS.

**Use of Computer-Processed Data.** We reviewed the financial data used by personnel at the DFAS Centers to prepare the DBOF Statement of Operations. Most of that data originated from various financial systems. Although we relied on the data, we did not test the reliability of the data. We plan to evaluate the

## Appendix A. Scope and Methodology

---

reliability of computer-processed data as part of the overall audit. The main objective of the overall audit is to determine whether expenses on the FY 1996 Consolidated Financial Statements of the DBOF are presented fairly in accordance with the other comprehensive basis of accounting described in Office of Management and Budget Bulletin No. 94-01, "Form and Content of Agency Financial Statements," and subsequent issuances.

**Audit Period, Standards, and Locations.** We performed our review of the presentation of financial data during the period June 1995 through April 1996. Our review was made in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. The results of our tests of internal controls will be included in our overall audit report. Appendix D lists the organizations we visited or contacted.

---

## **Appendix B. Summary of Prior Audits and Other Reviews**

The Inspector General, DoD, published three audit reports that discussed issues related to our audit. The Army Audit Agency issued a report that identified problems with how the DFAS Indianapolis Center prepared the Army FY 1995 Statement of Operations. The four reports are summarized below.

### **Inspector General, DoD**

Report No. 97-006, "Major Accounting and Management Control Deficiencies in the Defense Business Operations Fund in FY 1995," October 15, 1996, states that serious weaknesses in management control procedures, including inadequate guidance, contributed to the preparation of unreliable financial statements. Audits identified adjustments totaling \$7.7 billion that were attributable to faulty guidance. Weaknesses in the management control structure attributable to poor procedures occurred because DBOF accounting guidance was not always properly distributed, followed, up-to-date, or even developed in some cases. The report contained no specific recommendations, but advised management to develop and publish accounting guidance, ensure distribution to all users, and follow up to ensure consistent implementation.

Report No. 95-294, "Major Accounting Deficiencies in the Defense Business Operations Fund in FY 1994," August 18, 1995, states that many accounting problems at DoD organizations and on DBOF financial statements were directly attributable to deficient DBOF guidance. Audits identified 99 problems, resulting in auditor-recommended adjustments totaling \$13.3 billion, that were attributable to deficient DBOF guidance. Deficiencies in accounting guidance occurred principally because the procedures for distribution were faulty, implementation was irregular, and the guidance was insufficient or had not been developed. The report contained no specific recommendations, but advised management to develop and publish accounting guidance, ensure distribution to all users, and follow up to ensure consistent implementation.

Report No. 95-217, "Financial Statements for the Commissary Operations Fund, as of September 30, 1994," June 2, 1995, states that an opinion could not be rendered on the financial statements of the Commissary Operations Fund because the internal control structure, while improved, was not adequate to provide reasonable assurance that material misstatements would be prevented or detected in a timely manner. The report also indicates that the account balance of the Cost of Goods Sold, Intragovernmental, line item was materially misrepresented because operating expenses were reported on the wrong line item. The report did not contain any recommendations to change how operating expenses were reported in the financial statements.

## Army Audit Agency

Report No. AA 96-185, "Army Defense Business Operations Fund, Supply Management, FY 1995 Statement of Operations," February 1996, states that controls at the DFAS Indianapolis Center caused the Statement of Operations to be materially misstated. The DFAS Indianapolis Center did not comply with the Financial Management Regulation. Personnel did not properly establish the Allowance for Holding Gains and Losses account and the standard general ledger sub-accounts that would account for and report inventory gains and losses. Further, Cost of Goods Sold was not reduced for inventory losses realized for other than sales and did not include those losses in the Other Expenses line. Recommendations were made to correctly report expense account line items, add clarifying comments to the footnotes of the FY 1995 financial statements, and update the report mapping. Management agreed to update the report mapping and take other actions necessary to correctly report expense account line items. Clarifying comments to footnotes were made in those instances where the final FY 1995 financial statements were not changed.

---

## Appendix C. Major Expense Account Line Items and General Ledger Accounts

We reviewed the three expense account line items that comprised almost all of the costs in the FY 1995 Statement of Operations of reporting entities in the supply management business area. Specifically, we reviewed line 9, Program or Operating Expenses; line 10, Cost of Goods Sold; and line 14, Other Expenses. The following definitions describe the line items we reviewed and the major standard general ledger accounts that are to be used in calculating the line items.

**Line 9, Program or Operating Expenses.** Expenses incurred in conducting the normal activities of the entity classified by either program or major object class.

GLAC 6111 - Personnel Compensation-Civilian. The gross compensation for personal services rendered by Federal civilian employees and non-Federal employees.

GLAC 6117 - Transportation of Things. The expense of transporting things, excluding vendor transportation expenses.

GLAC 6120.2 - Purchased Services-Other-DBOF. Costs incurred for services received not otherwise classified at a DBOF organization.

GLAC 6121 - Supplies and Materials. Costs incurred for supplies and materials, including all supplies and materials consumed or used that do not meet capitalization criteria.

**Line 10, Cost of Goods Sold.** Costs applicable to goods sold to the public or other Federal entities, including the carrying value of commodities sold from stock.

GLAC 1529.1C - Purchases at Cost. The actual cost of inventory purchases.

GLAC 1529.1E - Material Returns - Credit Given. The amount of credit given for items returned.

GLAC 1529.3 - Allowance for Repairs. The summary account used to accumulate the estimated average cost to repair a damaged item, the estimated operating costs to accept and process a damaged item, and the amount of credit given for the exchange of a damaged depot level repairable item for a serviceable item.

GLAC 6500 - Cost of Goods Sold. The summary account used to accumulate the cost of goods sold from stock by DoD components or services sold to DoD components.

## Appendix C. Major Expense Account Line Item and General Ledger Accounts

---

**Line 14, Other Expenses.** Expenses incurred, but not reported on another expense account line.

**GLAC 6900 - Other Expenses.** Costs not otherwise classified as one of the other expenses.

**GLAC 7210 - Losses on the Disposition of Assets.** The loss on the disposition of assets and personal property.

**GLAC 7290 - Other Losses.** Losses of assets other than from disposition.

**GLAC 7291 - Inventory Losses or Adjustments.** Reductions in inventory that are not a result of sale, including inventory disposed of because it is considered as either excess or obsolete.

**GLAC 7293 - Other Miscellaneous Losses.** Losses which are not classifiable to a specific loss account.

**GLAC 7600 - Changes in Actuarial Liability.** The amount of increase or decrease in actuarial liability.

---

## **Appendix D. Organizations Visited or Contacted**

### **Office of the Secretary of Defense**

Office of the Under Secretary of Defense (Comptroller), Washington, DC  
Director of Revolving Funds, Office of the Deputy Comptroller (Program/Budget),  
Washington, DC  
Director of Accounting Policy, Office of the Deputy Chief Financial Officer,  
Washington, DC

### **Department of the Army**

Army Audit Agency, Alexandria, VA  
ATCOM (Aviation and Troop Command) Field Office, St. Louis, MO  
Huntsville Field Office, Huntsville, AL

### **Department of the Navy**

Naval Audit Service, Southeast Region, Virginia Beach, VA

### **Department of the Air Force**

Air Force Audit Agency, Wright-Patterson Air Force Base, OH

### **Other Defense Organizations**

Defense Commissary Agency, Fort Lee, VA  
Central Region, Little Creek Naval Amphibious Base, VA  
Commissary Store, Fort Knox, KY  
Midwest Region, Kelly Air Force Base, TX  
Headquarters, Defense Finance and Accounting Service, Arlington, VA  
Defense Finance and Accounting Service Cleveland Center, OH  
Defense Finance and Accounting Service Columbus Center, OH  
East Service Center, Fort Lee, VA  
West Service Center, Kelly Air Force Base, TX  
Defense Finance and Accounting Service Denver Center, CO  
Defense Finance and Accounting Service Indianapolis Center, IN  
Defense Finance and Accounting Service Kansas City Center, MO  
Defense Logistics Agency, Fort Belvoir, VA  
Defense Supply Center Columbus, OH

---

## **Appendix E. 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 to the Secretary of Defense (Public Affairs)

### **Department of the Army**

Auditor General, Department of the Army

### **Department of the Navy**

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

### **Department of the Air Force**

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

### **Other Defense Organizations**

Director, Defense Commissary Agency  
Director, Defense Contract Audit Agency  
Director, Defense Finance and Accounting Service  
Director, Defense Finance and Accounting Service Cleveland Center  
Director, Defense Finance and Accounting Service Columbus Center  
Director, Defense Finance and Accounting Service Denver Center  
Director, Defense Finance and Accounting Service Indianapolis Center  
Director, Defense Finance and Accounting Service Kansas City Center  
Director, Defense Logistics Agency  
Director, National Security Agency  
Inspector General, National Security Agency  
Inspector General, National Imagery and Mapping Agency

## **Non-Defense Federal Organizations**

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

## **Part III - Management Comments**

# Under Secretary of Defense (Comptroller) Comments



COMPTROLLER

OFFICE OF THE UNDER SECRETARY OF DEFENSE  
1100 DEFENSE PENTAGON  
WASHINGTON, DC 20301-1100



NOV - 5 1996

MEMORANDUM FOR DIRECTOR, FINANCE AND ACCOUNTING DIRECTORATE,  
OFFICE OF THE DOD INSPECTOR GENERAL

SUBJECT: Audit Report on Consistency in Reporting the Expense Account Line Items of the  
Defense Business Operations Fund (Project No 5FI-2016)

This is in response to the "Audit Report on Consistency in Reporting the Expense  
Account Line Items of the Defense Business Operations Fund (Project No 5FI-2016)," dated  
September 5, 1996.

I agree with the findings and recommendations except for the recommendation to  
categorize Cost of Goods and Services Sold as either "To the Public" or "Intragovernmental."  
Within the Defense Business Operations Fund (DBOF), the cost of goods and services sold do  
not differ based upon the customer (public or governmental). A financial statement categoriza-  
tion, therefore, of the cost of goods and services sold as either public or governmental could lead  
a user of the DBOF financial statements to infer that the cost of a good or service differed based  
upon the customer when that is not the case. More importantly, such an accounting treatment  
would create a compliance cost, without benefit, and add to the complexity of accounting and  
cost allocation.

The remainder of the findings and recommendations were helpful and have been or will be  
implemented. The efforts of the Inspector General and the DoD Component audit organizations  
in improving the operations of the DBOF are sincerely appreciated.

The point of contact for this matter is Mr. Thomas W. Short. Mr. Short may be reached  
by telephone at (703) 697-6875, DSN 227-6875 or e-mail at [shortt@ousdc.osd.mil](mailto:shortt@ousdc.osd.mil).

Alvin Fucker  
Deputy Chief Financial Officer

Attachment

**OFFICE OF THE UNDER SECRETARY OF DEFENSE (COMPTROLLER)  
COMMENT ON  
PROPOSED AUDIT REPORT  
"CONSISTENCY IN REPORTING THE EXPENSE ACCOUNT LINE ITEMS OF THE  
DEFENSE BUSINESS OPERATIONS FUND," PROJECT NO. 5FI-2016**

**RESPONSE TO RECOMMENDATIONS**

\*\*\*\*\*

**Recommendation 1.** The DoDIG recommends that the Under Secretary of Defense (Comptroller):

a. Revise DoD 7000.14-R, "Financial Management Regulation" Volume 11B, "Reimbursable Operations, Policy and Procedures-Defense Business Operations Fund," to conform with Office of Management and Budget Bulletin No. 94-01, "Form and Content of Agency Financial Statements." Specifically, require the following:

(1) Include standard general ledger account code 6900, Other Expenses, on line 14, Other Expenses, on Defense Business Operations Fund Accounting Report 1307;

**DoD Response:** Concur. Volume 11B of the "DoD Financial Management Regulation" is being revised. The revision will include standard general ledger account code 6900, Other Expenses, on line 14, Other Expenses, on Defense Business Operations Fund Accounting Report 1307.

(2) Present all the Defense Commissary Agency operating expenses on line 9, Program or Operating Expenses, on the Statement of Operations (and Changes in Net Position);

**DoD Response:** Concur. As recommended, the DoD Guidance on Form and Content of Financial Statements for FY 1996 Financial Activity has been revised to present all the Defense Commissary Agency operating expenses on line 9, Program or Operating Expenses, on the Statement of Operations. Additionally, Volume 11B of the "DoD Financial Management Regulation" is being revised. The revision to the monthly Defense Business Operations Fund (DBOF) Accounting Report 1307 Statement of Operations will report, consistent with the recommendation, Defense Commissary Agency operating expenses on the Statement of Operations rather than the Cost of Goods Sold.

(3) Categorize Cost of Goods and Services Sold as either "To the Public" and "Intragovernmental" on Defense Business Operations Fund Accounting Report 1307; and

**DoD Response:** Nonconcur. Within the DBOF, the cost of goods and services sold do not differ based upon the customer (public or governmental). A financial statement categorization, therefore, of the cost of goods and services sold as either public or governmental could lead a user of the DBOF financial statements to infer that the cost of a good or service differed based upon the customer when that is not the case. More importantly, such an accounting treatment would create a compliance cost, without benefit, and add to the complexity of accounting and cost allocation.

(4) Designate the specific standard general ledger account codes that are to be included on line 14, Other Expenses, on the Statement of Operations (and Changes in Net Position).

**DoD Response:** Concur. The specific standard general ledger account codes that are to be included as, Other Expenses, on the Statement of Operations are listed both in the instructions for the monthly DBOF Accounting Report 1307 financial reporting instructions and the DoD Form and Content Guidance. The listing contained in each is consistent with the other except that the instructions for Accounting Report 1307 financial statements also specify that general ledger account 6330, "Other Interest," be reported as "Other Expenses," although a separate line for interest expense is included in the format for the DoD Form and Content Guidance. The DBOF Accounting Report 1307 combines "Other Interest" with "Other Expenses" because there are few, if any, amounts recorded in account 6330. Therefore, a separate line for an account with no, or little, activity is not felt to be warranted.

b. Revise DoD Guidance on Form and Content of Financial Statements for FY 1996 Financial Activity to ensure that the guidance for preparing the Defense Business Operations Fund Statement of Operations (and Changes in Net Position) is the same as in DoD 7000.14-R, "Financial Management Regulation" volume 11B, "Reimbursable Operations, Policy and Procedures - Defense Business Operations Fund."

**DoD Response:** Concur. The DoD Guidance on Form and Content of Financial Statements for FY 1996 Financial Activity was revised to be consistent with guidance contained in Volume 11B, "Reimbursable Operations, Policy and Procedures - Defense Business Operations Fund," of DoD 7000.14-R. However, Volume 11B currently is under revision. As a result of comments received on its current content and proposed revision, current and/or proposed policies may be changed thus causing a divergence between it and the DoD Guidance on Form and Content.

**Recommendation 2.** The DoDIO recommends the Director, Defense Finance and Accounting Service, review the methodologies used by the Defense Business Operations Fund reporting entities and the Defense Finance and Accounting Service Centers to ensure consistency in calculating the expense account line items on the individual Statements of Operations (and Changes in Net Position). Specifically ensure the establishment and use of an allowance account in computing the cost of goods sold.

**DoD Response:** Concur. Representatives of the Defense Finance and Accounting Service met, on September 24, 1996, with DeCA, Comptroller personnel, and the DFAS-Columbus Center staff member who prepares the monthly DeCA Accounting Report 1307 financial report. Additionally, staff members of the DFAS Centers in Indianapolis, Cleveland, Kansas City, and Denver met on this issue at DFAS-Headquarters on October 1 and 2, 1996. The purpose of both the DeCA and the DFAS Center sessions was to review the methodologies that should be used in reporting allowance amounts and computing the cost of goods sold. DFAS-Headquarters will continue to schedule periodic working sessions with the DFAS Centers and other appropriate offices and conduct field visits if necessary to ensure that DFAS prepared financial reports and statements are in compliance with the DoD Financial Management Regulations, DoD Guidance on Form and Content of Financial Statements and other applicable DoD guidance. These working sessions will include elements to ensure that: (1) the methodologies used in reporting allowance amounts and computing the cost of goods sold are consistently implemented throughout the DFAS networks, and (2) that all appropriate expenses are properly recorded in the finance and accounting systems and reported correctly in the financial reports and statements.

**Audit Team Members**

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

**F. Jay Lane  
Richard B. Bird  
Carmelo G. Ventimiglia  
Gary S. Woodrum  
Theodore O. Baer  
N. Dale Gray  
Susanne B. Allen  
Helen S. Schmidt**