Audit Report

OFFICE OF THE INSPECTOR GENERAL

AIR NATIONAL GUARD FINANCIAL REPORTS ON THE NATIONAL GUARD AND RESERVE EQUIPMENT APPROPRIATION

Report No. 98-040

December 16, 1997

Department of Defense

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Acronyms

DFAS	Defense Finance and Accounting Service
NGREA	National Guard and Reserve Equipment Appropriation

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
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ARLINGTON, VIRGINIA 22202

December 16, 1997

MEMORANDUM FOR DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE

SUBJECT: Audit Report on Air National Guard Financial Reports on the National Guard and Reserve Equipment Appropriation (Report No. 98-040)

We are providing this audit report for review and comment. We performed this audit in response to the Chief Financial Officers Act of 1990 and the Federal Financial Management Act of 1994.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The Director, Defense Finance and Accounting Service Denver Center, did not comment on a draft of this report. We request that the Director provide comments on the final report by February 17, 1998.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Ms. Mary Lu Ugone, Audit Program Director, at (703) 604-9049 (DSN 664-9049); Ms. Dianna J. Pearson, Audit Project Manager, at (703) 604-9063 (DSN 664-9063); or Mr. Scott S. Brittingham, Audit Team Leader, at (703) 604-9068 (DSN 664-9068). See Appendix E for the report distribution. The audit team members are listed inside the back cover.

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Office of the Inspector General, DoD

Report No. 98-040 **December 16, 1997**
(Project No. 7RE-2006)

Air National Guard Financial Reports on the National Guard and Reserve Equipment Appropriation

Executive Summary

Introduction. The audit was performed in response to Public Law 101-576, "Chief Financial Officers Act of 1990," and Public Law 103-356, "Federal Financial Management Act of 1994." Public Law 101-576 established requirements for Federal organizations to submit audited financial statements to the Director, Office of Management and Budget. Public Law 103-356 requires DoD and other Government agencies to prepare consolidated financial statements for FY 1996 and each succeeding year.

In 1981, Congress established the National Guard and Reserve Equipment Appropriation to provide the equipment needed to maintain the readiness of the National Guard and Reserve units. In FY 1996, the Air National Guard received a total of $260.4 million for National Guard and Reserve Equipment programs. The Defense Finance and Accounting Service Denver Center prepares the financial reports for the Air National Guard by consolidating financial data for the operating budget organizations receiving the National Guard and Reserve Equipment Appropriation for various programs.

Audit Objectives. The overall audit objective was to evaluate the accuracy and completeness of FY 1996 financial information that the Defense Finance and Accounting Service Denver Center reported for the National Guard and Reserve Equipment Appropriation of the Air National Guard. Also, we determined the effect of noncompliant actions on the FY 1997 financial statements, assessed compliance with laws and regulations, and reviewed the management control program as it related to the overall audit objective.

Audit Results. The Defense Finance and Accounting Service Denver Center did not accurately present the financial data that the reporting organizations for the National Guard and Reserve Equipment Appropriation submitted for inclusion in the consolidated report on budget execution and adjusted trial balance. As a result, the FY 1996 consolidated report on budget execution for the National Guard and Reserve Equipment Appropriation for the Air National Guard is understated by $47 million for undelivered orders; overstated by $47 million for accounts payable; and understated for refunds due by $24 million. Additionally, unless the Defense Finance and Accounting Service Denver Center accurately reports financial data, the FY 1997 financial statements will also be incorrect. The results of the review of the management control program are in Appendix A.

Summary of Recommendations. We recommend that the Director, Defense Finance and Accounting Service Denver Center, report financial data as the reporting organizations submitted for the National Guard and Reserve Equipment Appropriation, unless documentation exists to support changes or adjustments; footnote abnormal balances on financial reports; and implement management controls for the consolidation process. We also recommend that the Defense Finance and Accounting Service Denver Center record and report credits due for progress payments, as applicable, and include the credits in financial data submitted for the financial statements.

Management Comments. We issued a draft of this report on September 26, 1997. The Director, Defense Finance and Accounting Service Denver Center, did not comment on a draft of this report. Therefore, we request the Director, Defense Finance and Accounting Service Denver Center, to provide written comments by February 17, 1998.

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Part I - Audit Results

Audit Background

The audit was performed in response to Public Law 101-576, "Chief Financial Officers Act of 1990," and Public Law 103-356, "Federal Financial Management Act of 1994." Public Law 101-576 established requirements for Federal organizations to submit audited financial statements to the Director, Office of Management and Budget. Public Law 103-356 requires DoD and other Government agencies to prepare consolidated financial statements for FY 1996 and each succeeding year. The consolidated DoD financial statements for FY 1996 included the financial data for the reporting entity entitled "Other Defense Organizations." The "Other Defense Organizations" entity includes the financial statements for that portion of Department 97* funds, to include the National Guard and Reserve Equipment Appropriation (NGREA), which is allocated to the Military Departments. See Appendix C for more details on the NGREA.

NGREA for the Air National Guard. The audit of the NGREA for the Air National Guard is the last of a series of reports on the NGREA. Appendix B lists the previous seven reports issued on the NGREA.

NGREA Accounting Responsibilities. The Under Secretary of Defense (Comptroller) made the Defense Finance and Accounting Service (DFAS) responsible for accounting support within DoD. The DFAS Denver Center provides accounting support for the operating budget activities of the Air National Guard NGREA.

NGREA Reporting Responsibilities. The DFAS Denver Center prepares the financial reports for the Air National Guard NGREA by consolidating financial data for operating budget account numbers that receive NGREA for specific programs. Both DFAS Denver Center operating locations and Air National Guard bases provide financial reporting for the 74 operating budget account numbers that received NGREA for budgeted programs.

Trial Balance. The DFAS Denver Center submits monthly trial balances using proprietary accounts to the DFAS Indianapolis Center. The DFAS Denver Center uses formulas to verify and adjust, as necessary, trial balance accounts to the report on budget execution.

Report on Budget Execution. The DD Form 1176, "Report on Budget Execution," is a monthly report designed to show, on a consistent basis and in practicable detail, the status of budgetary resources and related financial data. The DFAS centers prepare the report on budget execution for all appropriated funds. The report on budget execution shows the current status of funds for each appropriation in budgetary terms. Appendix D shows budgetary terminology associated with the report on budget execution.

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*The Department of the Treasury uses department code "97" to identify appropriations for the Office of the Secretary of Defense. The Military Departments also receive Department 97 appropriations, including the National Guard and Reserve Equipment Appropriation.

Status of Funds Report. The DFAS Denver Center uses the status of funds report to produce the report on budget execution and the adjusted trial balance. The DFAS Denver Center consolidates the status of funds report for financial data reported for the NGREA for the Air National Guard from multiple reports generated at the operating budget account numbers level as discussed below.

Database Transfer. Each NGREA reporting organization is required to submit a database transfer to DFAS Denver Center for fiscal yearend consolidation into the status of funds report. The database transfer, which is listed by operating budget account number, includes the yearend balance for accrued expenditures unpaid and unliquidated obligations outstanding. The database transfer also shows the cumulative balances for budget authority, gross obligations, and accrued expenditures paid.

Merged Accountability and Fund Reporting Reconciliation. The merged accountability and fund reporting reconciliation provides the financial data for disbursements and accrued expenditures paid by fiscal year and by program. In addition, the report shows differences between amounts posted by the DFAS Denver Center and the accounting station.

General Ledger Accounting Control. Key Accounting Requirement No. 1, "General Ledger Control and Financial Reporting," requires that accounting systems have general ledger control and maintain an appropriate account structure approved by DoD. The DFAS Denver Center uses data from the report on budget execution to produce the Air National Guard trial balances because supporting accounting systems are not complete general ledger accounting control systems.

Audit Objectives

The overall audit objective was to evaluate the accuracy and completeness of FY 1996 financial data that the DFAS Denver Center reported for the Air National Guard NGREA. Also, we determined the effect of noncompliant actions on FY 1997 financial statements, assessed compliance with laws and regulations, and reviewed the management control program as it related to the overall audit objective. See Appendix A for a discussion of the audit scope and methodology and the review of the management control program.

Financial Reports for the National Guard and Reserve Equipment Appropriation for the Air National Guard

The DFAS Denver Center did not accurately present the financial data that the reporting organizations for NGREA submitted for inclusion in the consolidated report on budget execution and adjusted trial balance. The report on budget execution is not accurate because the DFAS Denver Center did not:

- provide adequate disclosure for abnormal balances;
- compute accounts payable consistently;
- implement adequate controls for out-of-balance conditions noted during the consolidation process; and
- record and report credits due for a progress payment for inclusion in the financial statements.

As a result, the FY 1996 consolidated report on budget execution for the Air National Guard NGREA is understated by $47 million for undelivered orders and overstated by $47 million for accounts payable. Additionally, refunds due are understated by $24 million. Further, unless the DFAS Denver Center accurately reports financial data, the FY 1997 financial statements will also be incorrect.

DoD Financial Management Requirements

Key Accounting Requirements. The DoD 7000.14-R, "DoD Financial Management Regulation," volume 1, "General Financial Management Information, Systems, and Requirements," May 1993, requires DoD accounting systems to comply with 13 key accounting requirements. The key accounting requirements are composites of requirements of the General Accounting Office, the Office of Management and Budget, the Department of the Treasury, and DoD. Key Accounting Requirement No. 5, "Accrual Accounting," requires that Defense organizations record the amount of accrued expenditures only when the amount is supported by prescribed documentary evidence on the basis of the initial documentation received. The regulation also states that an entry to record accrued expenditures unpaid in budgetary accounts requires a corresponding entry to record accounts payable in proprietary accounts.

Budgetary and Proprietary Accounts. Almost every transaction affecting the use of Federal funds should be recorded both in budgetary accounts and proprietary accounts. Proprietary accounting records reflect changes in assets, liabilities, and equity of the Federal Government based on the following relationship:

Assets = Liabilities + Equity.

Budgetary accounting tracks and controls budgetary resources and the status of those resources, based on the following relationship:

Budgetary Resources = Status of Budgetary Resources.

For example, when an organization receives and accepts orders for goods or services, the organization has expended its authority for that amount and incurred a liability. At that point, the organization is required to record both proprietary and budgetary entries. The organization increases accounts payable to reflect the liability incurred for the goods or services. Also, the organization increases accrued expenditures unpaid to reflect the reduction in budget authority and decreases undelivered orders, reducing the amount of unliquidated obligations outstanding.

Reporting Differences for the Air National Guard

The DFAS Denver Center did not accurately present the financial data that the reporting organizations for NGREA submitted for inclusion in the consolidated report on budget execution and the adjusted trial balance. The reporting organizations reported an undelivered orders balance of $191 million, but the DFAS Denver Center reported an undelivered orders balance of $144 million.

Abnormal Accounts Payable Balance. Based on the data that the organizations submitted, the accounts payable contained a debit balance of $9.4 million, which is an abnormal balance. The abnormal accounts payable balance resulted from disbursements charged without a corresponding liability to match the disbursement.

The DFAS Indianapolis Center required the identification and correction of abnormal balances, including debit balances in liability accounts, before submission of the September 30, 1996, yearend trial balances. Abnormal balances remaining on reports require footnotes with detailed explanations stating the sources, the circumstances involved, and the actions underway to resolve the condition, including the estimated completion dates.

DFAS Denver Center Standard Computation of Accounts Payable. The DFAS Denver Center computes accounts payable using the accrued expenditures unpaid reported in the database transfer as the base amount. The DFAS Denver Center reduces the base amount by the difference between disbursements DFAS charged the appropriation and amount of accrued expenditures paid. The adjustment is referred to as the merged accountability and fund reporting

adjustment. Generally, disbursements are for the payment of a liability. Disbursements reduce the "Fund Balance With Treasury" and, therefore, reduce accounts payable. If the balance of accrued expenditures unpaid is not equal to or greater than the merged accountability and fund reporting adjustment amount, the accounts payable balance will result in a negative balance on the report on budget execution and a debit balance on the adjusted trial balance.

The balances for undelivered orders and accounts payable that the DFAS Denver Center reported differed from the consolidated Air National Guard submission when both of the following conditions existed:

- the standard computation created a consolidated debit balance in accounts payable for the fiscal year, and

- the consolidated fiscal year obligated balance was greater than the fiscal year accounts payable debit balance.

The undelivered orders and accrued expenditures unpaid differed by the amount of the abnormal accounts payable balance. Examples of two computations for accounts payable follow.

FY 1992 Accounts Payable. For FY 1992, DFAS Denver Center reported an accounts payable balance of $0 in the report on budget execution and in the adjusted trial balance but based on the supporting documentation accounts payable should have shown an abnormal balance of $12.5 million. The DFAS Denver Center eliminated the abnormal balance by increasing the accrued expenditures unpaid by $12.5 million and reducing undelivered orders by $12.5 million.

For FY 1992, the Air National Guard NGREA was allocated to 9 programs managed by organizations reporting $15.8 million in undelivered orders. One program, the Tactical Air Control Systems Improvements Program, made up 99 percent of the abnormal balance. Therefore, DFAS Denver Center eliminated the abnormal balance by reducing the undelivered orders of other programs by $12.5 million, at the consolidated level. As of June 24, 1997, DFAS Columbus Center had verified credits due the Tactical Air Control Systems Improvements Program, totaling $12.2 million, and identified an additional $10.4 million for verification. The credits due will reduce the abnormal balance.

FY 1994 Accounts Payable. The FY 1994 accounts payable computation resulted in a normal credit balance of $42.2 million. Therefore, no discrepancies existed between accounts payable and undelivered orders that the organizations reporting for the NGREA submitted and the DFAS Denver Center reported on the report on budget execution.

Controls for Consolidation. The DFAS Denver Center did not provide documentation to support changes to financial data that reporting organizations submitted. The DFAS Denver Center should have footnoted abnormal balances that resulted during the consolidation process with detailed explanations. Appendix A also discusses the controls for out-of-balance conditions that resulted from consolidation of financial data.

Financial Data for the NGREA. The reporting organizations reported an undelivered orders balance of $191 million, but the DFAS Denver Center reported an undelivered orders balance of $144 million. Table 1 shows balances reported for undelivered orders based on the database transfer that the reporting organizations submitted and based on the report on budget execution that the DFAS Denver Center prepared for FY 1996.

Table 1. Balances for Undelivered Orders
(dollars in millions)

FY	Undelivered Orders Based on Database Transfer	Undelivered Orders Based on Report on Budget Execution	Decrease
1990	$ 0.87	$ 0.87	0.00
1991	30.37	21.60	($ 8.77)
1992	15.82	3.30	(12.52)
1993	18.27	0.07	(18.20)
1994	49.49	49.49	0.00
1995	41.11	33.90	(7.21)
1996	34.95	34.91	(0.04)
Total	**$190.88**	**$144.14**	**($46.74)**

Impact of Undelivered Orders on Accounts Payable. As Table 1 shows, the DFAS Denver Center reported undelivered orders balances that differed substantially from the balances that the Air National Guard reporting organizations submitted on the database transfer. The supporting documentation reviewed showed no justification to account for the reduction of the undelivered orders balances on the report on budget execution balance. Table 2 shows the accounts payable balances based on data that the organizations reported on the database transfer and based on the accounts payable that the DFAS Denver Center reported on the report on budget execution.

Table 2. Balances for Accounts Payable
(dollars in millions)

FY	Accounts Payable Based on Database Transfer	Accounts Payable Based on Report on Budget Execution	Increase
1990	($4.91)	($ 4.91)	0.00
1991	(8.77)	0.00	$ 8.77
1992	(12.51)	0.00	12.51
1993	(18.21)	0.00	18.21
1994	42.23	42.23	0.00
1995	(7.21)	0.00	7.21
1996	(0.04)	0.00	0.04
Total	**($9.42)**	**$37.32**	**$46.74**

As stated, DFAS Denver Center is required to provide footnotes for abnormal balances. The DFAS Denver Center provided a footnote for the abnormal balance in FY 1990, stating that the abnormal balance was the result of an intransit disbursement and reconciliation differences for the organizations reporting for the NGREA. The DFAS Denver Center should have provided footnotes for FYs 1991 through 1993 and FYs 1995 and 1996, explaining in detail the reasons for the abnormal FY balances, and should continue to footnote abnormal balances in the future.

Impact of Undelivered Orders on the Trial Balance. The appropriated capital, a proprietary account, is affected by a reduction in undelivered orders because "undelivered orders" is one of the budgetary accounts that DFAS Denver Center uses to compute appropriated capital in the adjusted trial balance. Any change to accrued expenditures directly impacts accounts payable. Table 3 summarizes the budgetary and proprietary entries that the reporting differences directly created.

Table 3. Budgetary and Proprietary Entries
(dollars in millions)

Accounts	Debit	Credit
Undelivered Orders	$47 million	
Accrued Expenditures Unpaid		$47 million
Appropriated Capital	$47 million	
Accounts Payable		$47 million

Based on budgetary and proprietary entries required for the difference between financial data that reporting organizations submitted and that DFAS Denver Center reported, the net impact is that undelivered orders are understated by $47 million and accounts payable are overstated by $47 million.

Credit Due for a Progress Payment. The DFAS Denver Center operating location did not include or designate a $24 million credit due to the Air National Guard for a progress payment in the database transfer. The DFAS Columbus Center, which prorates progress payments, charged a progress payment to the Aeronautical Systems Command, Wright Patterson Air Force Base, which received NGREA to acquire equipment for the Air National Guard. Based on the database transfer that the operating location submitted, the Aeronautical Systems Command had exceeded its budget authority, as shown below.

Budget Authority	$300.5 million
Accrued Expenditures (paid and unpaid)	318.7 million
Unliquidated Obligations Outstanding	(18.4) million

The DFAS Denver Center included the negative unliquidated obligation of $18.4 million in the report on budget execution without determining the following about the abnormal balance. Instead of exceeding its budget authority by

$18.4 million, as the records indicate, the Aeronautical Systems Command actually had a $5 million balance of undelivered orders and the unobligated balance of $106,000. The difference, or the appearance of the negative balance, was attributed to the $24 million progress payment credit that the operating location had not recorded or reported. As a result, the balances of the report on budget execution for undelivered orders and refunds due are both understated by $24 million. Additionally, the appropriated capital account is understated by $24 million. If the operating location had recorded the credit due for the progress payment, the data submitted would have better reflected the financial position of the NGREA of the Air National Guard.

Although the financial records do not reflect the financial position of the appropriation, the Aeronautical Systems Command orders are not impacted by the credit due reflected at the appropriation level. The DFAS recorded the $24 million progress payment and charged the progress payments to account 9940. When a progress payment is charged to account 9940, a negative unliquidated obligation is automatically created because the contract obligation is established for the project funded for the related procurement. The Aeronautical Systems Command had contract obligations of $201.1 million and disbursements of only $200.9 million. According to the DFAS Denver Center operating location, the Aeronautical Systems Command did not exceed its budget authority because the $24 million charge to account 9940 represents a "paper" credit, or a refund due the Aeronautical Systems Command.

Classification of Credits for Progress Payments. The DoD Guidance on Form and Content of Financial Statements for FY 1996 Financial Activity states that progress payments made by general funds are to be classified as advances and prepayments. The DFAS Denver Center did not report the progress payment for $24 million on either the report on budget execution or the adjusted trial balance. If the Air National Guard had received the credit, the Fund Balance With Treasury would increase by $24 million. Because the financial records did not reflect the credit, the obligated balance for the program showed a negative balance of $18 million.

Summary

The DFAS Denver Center has a responsibility to ensure that it accurately presents in the financial statements the data that the reporting organizations submit. The undelivered orders balance represents the amount of goods and services ordered and obligated but not received. Adjustments to reported balances are of no value if they do not represent the financial and budget activity of the Air National Guard. Reporting abnormal accounts payable balances and providing footnotes, with detailed explanations, is of more value to the Air National Guard than reporting financial data that do not reflect transactions at the detailed level. By adjusting undelivered orders, the DFAS Denver Center presented inaccurate financial data for orders due to the Air National Guard. The DFAS Denver Center must present the data as submitted and provide disclosures, as necessary, on financial data with abnormal balances.

Recommendations for Corrective Action

We recommend that the Director, Defense Finance and Accounting Service Denver Center:

1. Report financial data as the reporting organizations submitted for the National Guard and Reserve and Equipment Appropriation, unless documentation exists to support changes or adjustments to the data.

2. Implement management controls for the consolidation process, especially for out-of-balance conditions that result from the consolidation of financial data.

3. Record and report credits due for progress payments, as applicable, and include the credits in financial data submitted for the financial statements.

Management Comments Required

The Director, Defense Finance and Accounting Service Denver Center, did not respond to the draft of this report. We request the Director, Defense Finance and Accounting Service Denver Center, provide comments on this final report.

Part II - Additional Information

Appendix A. Audit Process

Scope and Methodology

Scope. We reviewed the FY 1996 Air National Guard report on budget execution, which showed total budgetary resources of $651.9 million, and the adjusted trial balance that the DFAS Denver Center submitted for the National Guard and Reserve Equipment Appropriation (NGREA). We performed the audit in response to Public Law 101-576, "Chief Financial Officers Act of 1990," which established requirements for Federal organizations to submit audited financial statements to the Director, Office of Management and Budget. Appendix C provides details on the NGREA.

Methodology. We reviewed the process that the DFAS Denver Center used to prepare the FY 1996 report on budget execution and the adjusted trial balance for the Air National Guard. We also reviewed the FY 1996 Status of Funds report and the financial data submitted on the database transfer from the General Accounting and Finance System, referred to as the "BQ" at the base level, and the Merged Accounting and Fund Reporting System Reconciliation.

Use of Computer-Processed Data. We relied on computer-processed data from the DFAS Denver Center Status of Funds System; the Merged Accountability and Fund Reporting System; and the General Accounting and Finance System without confirming the reliability of the data. We did not establish the reliability of the data because we reviewed the process that the DFAS Denver Center used to prepare the FY 1996 Air National Guard reports on budget execution for the NGREA. Therefore, not establishing the reliability of the financial data did not materially affect the results of our audit.

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

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

Management Control Program

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, requires DoD organizations to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and to evaluate the adequacy of those controls.

Scope of Review of the Management Control Program. We reviewed the management controls over the process that the DFAS Denver Center used to prepare the Air National Guard NGREA reports on budget execution and trial balances. We also reviewed management's self-evaluation applicable to the controls over that process.

Adequacy of Management Controls. We identified material management control weaknesses, as defined by DoD Directive 5010.38, for the DFAS Denver Center. The DFAS Denver Center had not implemented management controls to comply with Key Accounting Requirement No. 5, which requires that the amount of accrued expenditures be recorded only when supported by prescribed documentary evidence on the basis of documentation received. Further, the DFAS Denver Center had not implemented management controls over the consolidation process, including out-of-balance conditions resulting from the data consolidation. Additionally, management controls did not prevent DFAS Denver Center from reporting a credit due for a progress payment as a negative unliquidated obligation in the financial reports. All the recommendations, if implemented, will correct the weaknesses. We will provide a copy of the report to the senior official in charge of management controls for the DFAS Denver Center.

Adequacy of Management's Self-Evaluation. The DFAS Denver Center stated in the Annual Statement of Assurance for FY 1996 that the Merged Accountability and Fund Reporting System Reconciliation was a material weakness because it had differences between departmental and installation level records. The statement adds that installation level accounting was not effectively using the DFAS Denver Center cumulative data listing to perform the required reconciliation of departmental and installation level records for disbursements.

The DFAS Denver Center identified accounting and reporting for the NGREA as part of an assessable unit but assigned only a medium level of risk to that assessable unit and, therefore, did not perform an evaluation of the unit. Because the DFAS Denver Center did not perform the evaluation, the DFAS Denver Center did not identify or report the material management control weaknesses identified by the audit.

Appendix B. Prior Audits on the National Guard and Reserve Equipment Appropriation

Inspector General, DoD, Report No. 97-215, "Reporting of Accounts Payable for the National Guard and Reserve Equipment Appropriation on the Other Defense Organizations Portion of the FY 1996 Financial Statements," September 18, 1997. The report states that the DFAS Denver Center correctly reported accounts payable for open and closed appropriations. The DFAS Cleveland Center and the DFAS Indianapolis Center did not report accounts payable remaining on closed appropriations for the NGREA. As a result, accounts payable for the NGREA are understated by $12.8 million on the "Other Defense Organizations" portion of the FY 1996 DoD financial statements. The report recommends that the Under Secretary of Defense (Comptroller) revise the DoD "Guidance on Form and Content of Financial Statements for FY 1997 Financial Activity" to specify the reporting requirements of accounts payable for closed appropriations. The Under Secretary of Defense (Comptroller) did not comment on the report.

Inspector General, DoD, Report No. 97-201, "Navy and Marine Corps Reserve Financial Reports on the National Guard and Reserve Equipment Appropriation," July 30, 1997. The report states that the FY 1996 reports on budget execution for the Navy and Marine Corps Reserve NGREA are not fully supported with source documentation. As a result, reports on budget execution for the NGREA could not be verified, and the FY 1996 Navy and Marine Corps Reserves ending trial balances may be unreliable.

The report recommends that the DFAS Cleveland Center document the audit trail process for report preparation in accordance with Key Accounting Requirement No. 8, reconcile discrepancies between source documents and Marine Corps Reserve NGREA transactions at the Naval Air Systems Command for FY 1996, and provide the DFAS Kansas City Center access to and a method for identifying Marine Corps Reserve transactions within the DFAS accounting system. The report also recommends that the DFAS Kansas City Center provide complete financial data for the Marine Corps Reserve NGREA after obtaining access to Marine Corps Reserve transactions in the DFAS Cleveland Center accounting system.

The DFAS concurred with the intent of all the recommendations and indicated that corrective actions are being taken. However, the DFAS stated that the DFAS Kansas City Center must rely on the Standard Accounting, Budgeting, and Reporting System to perform its increased financial reporting responsibilities, rather than using the access to the DFAS Cleveland Center Standard Accounting and Reporting System. The DFAS Cleveland Center stated that the Standard Accounting, Budgeting, and Reporting System would provide complete financial reporting capability for the Marine Corps Reserve NGREA.

The report states that the DFAS Kansas City Center Standard Accounting, Budgeting, and Reporting System will not provide the complete financial reporting capability required for DFAS Kansas City Center for the Marine Corps Reserve NGREA. The Navy received 83 percent of Marine Corps Reserve NGREA, which is accounted for within the Standard Accounting and Reporting System. Unless the Navy inputs all of its Marine Corps NGREA transactions into the Standard Accounting, Budgeting, and Reporting System the DFAS Kansas City Center can only account for 17 percent of the Marine Corps Reserve NGREA. The report requested that DFAS Headquarters provide additional comments.

Inspector General, DoD, Report No. 97-153, "Marine Corps Reserve Financial Reports on the National Guard and Reserve Equipment Appropriation," June 9, 1997. The report states that the FY 1996 Marine Corps Reserve trial balance for the NGREA is misstated. As a result, the "Fund Balance With Treasury" account is overstated by $8.4 million, and the Appropriated Capital account is overstated by $8.6 million on the FY 1996 Marine Corps Reserve trial balance.

The report recommends that the DFAS Cleveland Center establish management controls to ensure that certified Marine Corps Reserve report on budget execution data are used to prepare the trial balance and report on budget execution and make appropriate disclosures when certified Marine Corps Reserve budget execution data are not used. Both the DFAS Cleveland Center and DFAS Kansas City Center are establishing management controls and have initiated corrective measures to ensure that certified yearend reports are used.

Inspector General, DoD, Report No. 97-116, "Allegations of Improper Accounting for the National Guard and Reserve Equipment Appropriation at the Army National Guard," March 31, 1997. The report states that the Army National Guard made material accounting adjustments, reducing recorded obligations against the FY 1991 appropriation, before submitting FYs 1994 and 1995 budget execution reports. In addition, the Army National Guard obligated $13.6 million of FY 1996 appropriated funds to offset apparent FY 1991 overobligations but did not report a potential Antideficiency Act violation.

The report recommends that the Army National Guard review and immediately revise the practices that Army National Guard officials used to make inappropriate accounting adjustments. Additionally, the report recommends that the Army National Guard develop and implement procedures to ensure that material accounting adjustments to recorded budget transactions are properly authorized, properly approved, and adequately documented. The report also recommends that the Army National Guard establish management control procedures to ensure proper reporting of potential Antideficiency Act violations.

The Army National Guard agreed with all the recommendations except establishing management control procedures to ensure proper reporting of potential Antideficiency Act violations. The Army National Guard stated that it complied with the appropriate regulatory requirements because a reconciliation of FY 1991 funds did not disclose any financial transaction that created a potential

overobligation. The decision not to report the overobligations was based on the likelihood, later confirmed, that accounting errors were responsible for the apparent overobligations.

Inspector General, DoD, Report No. 97-047, "Consolidated Financial Report on the National Guard and Reserve Equipment Appropriation for the Army National Guard," December 13, 1996. The report states that the Army National Guard did not properly record and report transactions in the general ledger. The Army duplicated reporting of military equipment, misstated liabilities, and incorrectly used a budgetary account. In addition, the Army National Guard did not record accounts payable upon evidence of equipment receipts. As a result, the September 30, 1995, general ledger account balances for the Army National Guard contained the following misstatements:

o account 1722, "Construction in Progress-Contractor," was overstated by $427.1 million;

o account 2111, "Accounts Payable-Government-Current," was overstated by $5.4 million; account 2113, "Accounts Payable-Public-Current," was understated by $321,000; and account 4910, "Accrued Expenditures Unpaid-Direct Program," was overstated by $5.1 million; and

o account 4584, "Anticipated Earned Authority-Defense Business Operations Fund," was incorrectly used to record allotted authority of $323.3 million.

The report recommends that the Army National Guard make adjusting entries to correct general ledger account balances and establish adequate controls to prevent duplicate recording and reporting of military equipment, to record liabilities for military equipment received in advance of payment, to record accounts payable only for transactions representing legitimate Army National Guard liabilities, and to reclassify allotments received. The National Guard Bureau concurred with recommendations to make adjusting accounting entries to correct various proprietary and budgetary account balances, and corrective actions were taken.

The National Guard Bureau partially concurred with the recommendation to develop and implement procedures to prevent duplicate recording and manage liabilities for military equipment purchased with NGREA funds. The National Guard Bureau stated that the Army lacked the visibility over receipt of equipment needed to record the liabilities. The National Guard Bureau had since taken corrective action to develop state level general ledger processes and is working with the Army Audit Agency and the DFAS Indianapolis Center to develop state level general ledger processes in the State Accounting, Budget Execution, and Reservation System. Additionally, the processes will include the development of a handbook that State personnel will use in posting property and equipment general ledger accounts.

Inspector General, DoD, Report No. 97-044, "Army National Guard Military Equipment," December 11, 1996. The report states that the Army National Guard materially misstated military equipment balances included in the FY 1995 Army financial statements. The Army National Guard:

- recorded and reported military equipment items that were below the Army capitalization threshold and, therefore, should have been expensed and

- misstated military equipment in transit as equipment in use.

As a result, the military equipment account was overstated by $9.1 million. Additionally, account 1762, "Equipment in Use," was overstated by $1.2 billion and account 1770, "Equipment in Transit," was understated by $1.2 billion.

The report recommends that the Army National Guard record and report the value of military equipment using established capitalization thresholds, make specific accounting entries to accurately record and classify military equipment account balances in the general ledger, and document procedures for recording and reporting military equipment transactions. The report also recommends that the Deputy Chief of Staff for Logistics provide general ledger account balances for military equipment to the Army National Guard accounts 1762 and 1770 and that DFAS Indianapolis Center make appropriate accounting entries to accurately classify Army National Guard military equipment in the Army general ledger.

The National Guard Bureau concurred with recommendations to record and report the value of military equipment using established capitalization thresholds, make accounting entries to accurately record and classify military equipment account balances in the general ledger, and document procedures for recording and reporting military equipment transactions. The DFAS Indianapolis Center nonconcurred with the recommendation that it make appropriated entries to accurately classify Army National Guard military equipment in the Army general ledger, stating that it could not make correcting entries to the Army general ledger. However, DFAS Indianapolis Center would advise the Army National Guard and request revisions if the data are not consistent with Army guidance.

Inspector General, DoD, Report No. 97-025, "Consolidated Financial Report on the National Guard and Reserve Equipment Appropriation for the Army Reserve," November 19, 1996. The report states that the DFAS Indianapolis Center omitted pertinent financial information in preparing the FY 1995 Army Reserve trial balance for the NGREA. As a result, the expenses on the FY 1995 trial balance are understated, and equity on the FY 1996 financial statements will be overstated by $70.1 million. The report recommends that the DFAS Indianapolis Center include all valid limitation codes for the Army Reserve in the general ledger database extraction program, establish management controls to verify the completeness of information extracted for financial statements, and adjust the appropriated capital account by $70.1 million on the Army reserve FY 1996 trial balance for the NGREA.

The DFAS Indianapolis Center agreed to include all valid limitation codes for the Army Reserve in the general ledger database extraction program and to establish management controls to ensure the completeness of the information extracted for the financial statements. The DFAS Indianapolis Center partially concurred with the recommendation to adjust the appropriated capital account by $70.1 million because the inclusion of the valid limitation codes will eliminate the need to adjust the appropriated capital account by $70.1 million.

Appendix C. The National Guard and Reserve Equipment Appropriation

The NGREA is a multiyear DoD procurement appropriation available for obligation in the first 3 fiscal years. The NGREA allows an additional 5 years to disburse the obligations incurred during the first 3 years. For the reporting period that ended September 30, 1996 (consisting of FYs 1989 through 1996), Congress appropriated a total of $3.1 billion in NGREA funds to the Air National Guard. The following table shows the NGREA funds appropriated to the Air National Guard FY 1996 reporting period.

NGREA Funds for the Air National Guard
(dollars in millions)

Fiscal Year	NGREA
1989	$ 399.2
1990	236.7
1991	647.5
1992	558.0
1993	413.8
1994	339.9
1995	245.1
1996	260.4
Total	**$3,100.6**

Purpose of the NGREA. In 1981, Congress established NGREA to provide the equipment needed to maintain the readiness of the National Guard and Reserve units. Congress specifies the amount of NGREA funds that each Military Department should receive. The Chiefs of the Reserve and National Guard components within each of the Military Departments manage their respective portions of NGREA. The following six components comprise the National Guard and Reserve:

- Army National Guard,
- Air National Guard,
- Army Reserve,
- Navy Reserve,
- Air Force Reserve, and
- Marine Corps Reserve.

Fund Allocation Process. The Office of the Under Secretary of Defense (Comptroller) allocates the Air National Guard NGREA funds to the Assistant Secretary of the Air Force (Financial Management and Comptroller). The Assistant Secretary of the Air Force (Financial Management and Comptroller) allocates the funds to the Director, Air National Guard.

Appendix D. Definitions of Terms for Financial Reports

Budgetary and Proprietary Accounts. Office of Management and Budget Circular A-34 requires governmental agencies to submit reports on the budgetary status of their financial activity and related financial data. The DD Form 1176, "Report on Budget Execution," is a monthly report designed to show, on a consistent basis and in practicable detail, the status of budgetary resources and related financial data. The DFAS centers prepare the report on budget execution for all appropriated funds. The report on budget execution reflects the current status of funds for each appropriation in budgetary terminology and is used to verify and adjust, as necessary, the trial balance accounts. Budgetary accounts reflect the appropriation status from the time that the appropriation is realized until it is spent. Proprietary accounts reflect the status of assets, liabilities, equity, revenue, and expenses and are shown on the trial balance. Budgetary accounts and the associated proprietary accounts for the report on budget execution and the trial balance are shown as follows.

1. **Accounts Payable.** "Accounts payable" is the proprietary account showing amounts that a Federal entity owes for goods and services received from nonfederal entities.

2. **Accrued Expenditures Paid.** Accrued expenditures paid is the budgetary account that matches the proprietary account "funds disbursed."

3. **Accrued Expenditures Unpaid.** Accrued expenditures unpaid is the budgetary account that matches the proprietary account "accounts payable." It represents the dollar value of goods and services received for which payment has not been made.

4. **Accrued Liabilities.** "Accrued liabilities" is the proprietary account showing amounts owed for items received, services received, expenses incurred, assets acquired, construction performed, and amounts received but not earned.

5. **Appropriated Capital.** Appropriated capital is the proprietary account representing the net amount that Congress appropriated. It shows the difference between the "Fund Balance With Treasury" and the funded accounts payable.

6. **Appropriated Capital Used.** Appropriated capital used is the proprietary account showing the amount of appropriations used to finance expenses.

7. **Fund Balance With Treasury.** "Fund Balance With Treasury" is the proprietary account showing the aggregate amount of the entity's accounts with the Department of the Treasury for which the entity is authorized to make expenditures and pay liabilities.

8. **Gross Unpaid Obligations.** "Gross unpaid obligations" is the budgetary account showing the sum of undelivered orders and accounts payable, net of advances, prepayments, and refunds due. The amount represents the total amount of obligations, expended and unexpended, for which payment will be made.

9. **Undelivered Orders.** "Undelivered orders" is the budgetary account showing the amount of obligations incurred for which the related accrued expenditures and liabilities have not been incurred. An obligation represents the amount that will have to be disbursed in the future.

Appendix E. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Comptroller)
  Deputy Chief Financial Officer
  Deputy Comptroller (Program/Budget)
Assistant Secretary of Defense (Public Affairs)
Assistant Secretary of Defense (Reserve Affairs)
Director, Defense Logistics Studies Information Exchange

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

Chief, National Guard Bureau
  Director, Air National Guard
Director, Defense Contract Audit Agency
Director, Defense Finance and Accounting Service
Director, Defense Logistics Agency
Director, National Security Agency
  Inspector General, National Security Agency
Inspector General, Defense Intelligence Agency

Non-Defense Federal Organizations and Individuals

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

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

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

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