Audit Report

INTERNAL CONTROLS AND COMPLIANCE WITH LAWS AND REGULATIONS FOR THE DEFENSE COMMISSARY AGENCY FINANCIAL STATEMENTS FOR FY 1997

Report Number 98-158 June 17, 1998

Office of the Inspector General
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Acronyms

DeCA	Defense Commissary Agency
DFAS	Defense Finance and Accounting Service
IG	Inspector General
OMB	Office of Management and Budget
SF	Standard Form
SRD-1	Standard Finance System Redesigned 1
STANFINS	Standard Finance System

INSPECTOR GENERAL
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June 17, 1998

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

SUBJECT: Audit Report on Internal Controls and Compliance With Laws and Regulations for the Defense Commissary Agency Financial Statements for FY 1997 (Report No. 98-158)

We are providing this audit report for review and comment. Financial statement audits are required by the Chief Financial Officers Act of 1990 as amended by the Federal Financial Management Act of 1994. On February 28, 1998, we issued a disclaimer of opinion on the FYs 1997 and 1996 Financial Statements of the Defense Commissary Agency. We identified internal control weaknesses and instances of noncompliance with laws and regulations that merit management's attention. Part I of this report discusses material weaknesses in internal controls and noncompliance with laws and regulations. Part II of this report contains relevant appendixes for management use. We considered management comments on a draft of this report in preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The Defense Finance and Accounting Service did not comment on the draft of this report. Therefore, we request that the Director, Defense Finance and Accounting Service, provide comments on Recommendation 1 by July 17, 1998.

We appreciate the courtesies extended to the audit staff. For additional information on this report, please contact Mr. David F. Vincent at (703) 604-9110 (DSN 664-9110), e-mail <DVincent@DODIG.OSD.MIL>; or Ms. Barbara A. Sauls at (703) 604-9129 (DSN 664-9129), e-mail <BSauls@DODIG.OSD.MIL>. See Appendix G for the report distribution. A list of audit team members is on the inside back cover.

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Report No. 98-158 **June 17, 1998**
(Project No. 7FH-2042.01)

Internal Controls and Compliance With Laws and Regulations for the Defense Commissary Agency Financial Statements for FY 1997

Executive Summary

Introduction. Public Law 101-576, the "Chief Financial Officers Act of 1990," November 15, 1990, as amended by Public Law 103-356, the "Federal Financial Management Act of 1994," October 13, 1994, requires an annual audit of the financial statements of revolving funds such as the Defense Commissary Agency. Preparation of the Defense Commissary Agency financial statements is the responsibility of the Defense Finance and Accounting Service (DFAS). The Chief Financial Officers Act of 1990 prescribes the responsibility of management and auditors with respect to the financial statements, internal controls, and compliance with laws and regulations. Defense Commissary Agency management is responsible for establishing and maintaining internal control and complying with laws and regulations. Although the Defense Commissary Agency Consolidated Financial Statements for FYs 1997 and 1996 consisted of statements for Operations and Resale, we did not audit the Operations statements. As of September 30, 1997, the Defense Commissary Agency Resale Stock Fund reported assets of $429.8 million, liabilities of $374.9 million, and revenues of $5.1 billion.

Audit Objectives. Our overall objective was to determine whether the Defense Commissary Agency Consolidated Financial Statements for FYs 1997 and 1996 were presented fairly and in accordance with Office of Management and Budget Bulletin No. 94-01, "Form and Content of Agency Financial Statements," November 16, 1993, as modified by Office of Management and Budget Bulletin No. 97-01, "Form and Content of Agency Financial Statements," October 16, 1996. However, we limited our scope to the Defense Commissary Agency Resale Stock Fund. Additional objectives were to assess internal controls and compliance with laws and regulations as they relate to the financial statements and to follow up on corrective actions resulting from previous audits of the Defense Commissary Agency's financial statements.

Disclaimer of Opinion. We were unable to render an opinion on the Defense Commissary Agency Resale Stock Fund Consolidated Financial Statements for FYs 1997 and 1996. We did not receive the financial statements in a timely manner; therefore, we could not determine the accuracy and completeness of the data reported. Also, we were unable to observe a physical inventory at any commissary because the inventories were completed before we began audit work. Therefore, the scope of our work was limited. For the work we performed on the FY 1997 Defense Commissary Agency Resale Stock Fund Financial Statements, we identified significant deficiencies in the accounting systems and the lack of sound internal controls prevented the preparation of accurate financial statements. Our disclaimer of opinion was included in the financial statements transmitted by the Under Secretary of Defense (Comptroller) to the Office of Management and Budget.

Internal Controls. Internal controls for the FY 1997 Financial Statements of the Defense Commissary Agency Resale Stock Fund were not adequate. The DFAS Columbus Center's automated financial information systems created risks in the preparation of financial statements for the Defense Commissary Agency and the reconciliation of differences in deposits. Other reportable conditions existed in inventory accountability and the recording and reporting of expenses. See Part I.A. for the finding on deposit reconciliation and Appendix A for a discussion of management controls.

Compliance with Laws and Regulations. Noncompliance with laws and regulations continued to materially affect the reliability of the Defense Commissary Agency Consolidated Financial Statements. Financial management systems and internal controls did not completely or accurately disclose the financial condition of the agency, as required by title 31, U.S. Code. Financial management systems did not comply with Federal requirements for financial management systems; and the U.S. Government Standard General Ledger at the transaction level as required by the Federal Financial Management Improvement Act of 1996 and Office of Management and Budget Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993, as modified by Office of Management and Budget Bulletin No. 98-04, "Addendum to OMB Bulletin No. 93-06," January 16, 1998. The Standard Finance System, a general ledger system, and the Standard Finance System Redesigned 1, a disbursing system, did not provide reasonable assurance that Defense Commissary Agency financial statements were reliable. Also, DFAS was not in compliance with DoD Regulation 7000.14-R, the "DoD Financial Management Regulation." Specifically, DFAS excluded purchase discounts when recording Accounts Payable. Part I.B. is our report on compliance with laws and regulations. Appendix E lists the laws and regulations we reviewed.

Summary of Recommendations. We recommend that the Director, DFAS, consider, when studying alternative accounting systems to support the Defense Commissary Agency Resale function, a system that is compatible with the Defense Standard Disbursing System and the Defense Joint Accounting System. Also, we recommend that the Director, Defense Commissary Agency, clarify and standardize procedures for forwarding bank information to the DFAS Columbus Center to expedite the reconciliation of deposits.

Management Comments. The Director, Defense Commissary Agency, agreed to clarify and standardize procedures for forwarding bank information to the DFAS Columbus Center. See Part I for a discussion of management comments and Part III for the complete text of management comments. The Director, DFAS, did not respond to a draft of this report.

Audit Response. The comments from the Director, Defense Commissary Agency were responsive. We request the Director, DFAS, provide comments in response to the final report by July 17, 1998.

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Part I - Audit Results

Audit Background

Introduction. Public Law 101-576, the "Chief Financial Officers Act of 1990," as amended by Public Law 103-356, the "Federal Financial Management Act of 1994," October 13, 1994, requires financial statement audits of agencies such as the Defense Commissary Agency (DeCA) by the Inspector General (IG) and prescribes the responsibilities of management and auditors for the financial statements, internal controls, and compliance with laws and regulations. The Director, DeCA, is responsible for establishing and maintaining internal controls and for complying with laws and regulations applicable to DoD. Our responsibility is to render an opinion on those statements based on our work, and to determine whether internal controls were adequate and whether DeCA complied with laws and regulations. Appendix A discusses the scope and methodology, auditing standards, and accounting principles applicable to this audit. Appendix A also discusses our review of the FY 1997 Financial Statements of the DeCA Resale Stock Fund.

DeCA is responsible for the information in the DeCA Resale Stock Fund Financial Statements. The Statement of Financial Position and the Statement of Operations show the work of the DeCA Resale Stock Fund by comparing its assets, liabilities, revenues, and expenses as of the end of FY 1997. The following table identifies the major accounts reported on the FY 1997 Financial Statements of the DeCA Resale Stock Fund.

Major Accounts of the DeCA Resale Stock Fund as of September 30, 1997
(millions)

Asset Accounts	Balance
Fund Balance With Treasury	($148.8)
Funds Collected	$5,030.6
Funds Disbursed	($5,179.4)
Inventory Held for Sale, Net	$328.0
Liability Accounts	
Accounts Payable (Governmental)	$319.2
Revenue Accounts	
Revenue From Sales of Goods and Services	$5,097.5
Expense Account	
Cost of Goods Sold	$ 5,141.7

Accounting Functions and Responsibilities. The Defense Finance and Accounting Service (DFAS) Columbus Center performs accounting functions and prepares financial statements for DeCA. The DFAS Columbus Center operates under the control and direction of Headquarters, DFAS. Headquarters, DFAS and the DFAS Columbus Center jointly prepare the DeCA Financial Statements. The DFAS Columbus Center is responsible for entering information from DoD entities into the financial systems, operating and maintaining the financial systems, and ensuring the continued integrity of the information entered. DeCA is responsible for providing accurate financial information to DFAS Columbus Center.

Accounting Policies. The DeCA Resale Stock Fund Financial Statements for FYs 1997 and 1996 were to be prepared in accordance with the Office of Management and Budget (OMB) Bulletin No. 94-01, "Form and Content of Agency Financial Statements," November 16, 1993, as amended by OMB Bulletin No. 97-01, "Form and Content of Agency Financial Statements," October 16, 1996. Footnote 1 of the DeCA Resale Stock Fund FY 1997 financial statements discusses the significant accounting principles used to prepare the financial statements. See Appendix A for a more detailed discussion of accounting principles.

Disclaimer of Opinion. We were unable to render an opinion on the DeCA Consolidated Financial Statements for FYs 1997 and 1996. The Defense Commissary Agency Consolidated Financial Statements consisted of statements for Operations and Resale Stock Fund. We did not audit the financial statements for Operations. In addition, we did not receive the financial statements in a timely manner; therefore, we could not determine the accuracy and completeness of the data reported. Also, we were unable to observe a physical inventory at any commissary because the inventories were completed before we began audit work. Therefore, the scope of our work was limited. For the work we performed on the FY 1997 DeCA Resale Stock Fund Financial Statements, we found that significant deficiencies in the accounting systems and the lack of sound internal control prevented the preparation of accurate financial statements. Our disclaimer of opinion was included in the DeCA FY 1997 Financial Statements. Our final report will include the DeCA Financial Statements and our disclaimer of opinion.

Working Capital Fund. A working capital fund is a revolving fund that operates as an accounting entity. Each working capital fund has business areas or activity groups, such as DeCA Resale Stock Fund, that finance the purchase of inventory for resale items to be sold to commissary patrons. The DeCA Resale Stock Fund is a major business area of the DeCA Working Capital Fund, and requires no support from appropriated funds. Before FY 1992, DoD operated a number of commercial and industrial facilities under a revolving fund concept. In FY 1992, the revolving funds were consolidated to form the Defense Business Operations Fund. The IG, DoD, was responsible for auditing and rendering an opinion on the consolidated financial statements of the Defense Business Operations Fund. In December 1996, the Under Secretary of Defense (Comptroller) restructured the Defense Business Operations Fund into separate working capital funds.

Audit Objectives

Our overall objective was to determine whether the DeCA Consolidated Financial Statements for FYs 1997 and 1996 were prepared in accordance with OMB Bulletin No. 94-01, as amended by OMB Bulletin No. 97-01. Our scope was limited to the FY 1997 DeCA Resale Stock Fund. We also evaluated internal controls and compliance with laws and regulations as they related to the financial statements and followed up on corrective actions resulting from previous audits of the DeCA financial statements.

Part I. A. - Review of Internal Controls

Introduction

Audit Responsibilities. Our audit objective was to determine whether controls over transactions supporting the Inventory, Accounts Payable, and Revenue accounts in the FY 1997 Financial Statements of the DeCA Resale Stock Fund were adequate to ensure that the accounts were free of material error. In planning and performing our work, we evaluated internal controls at DeCA and DFAS Columbus Center. We performed this evaluation to:

- determine the auditing procedures necessary to render an opinion on the financial statements, and
- determine whether internal controls had been established and placed in operation.

Management Responsibilities. As the Chief Financial Officer, the Under Secretary of Defense (Comptroller) oversees all financial management activities for DoD programs and operations, including the accounting functions of DFAS. DeCA is responsible for managing its operations. Establishing and maintaining internal controls appropriate to the entity is an important responsibility of DeCA management. The objectives of internal controls are to provide management with reasonable, but not absolute, assurance that:

- transactions are properly recorded and accounted for to permit the preparation of reliable financial statements and to maintain accountability over assets;
- funds, property, and other assets are safeguarded against waste, loss, unauthorized use, and misappropriation; and
- transactions, including those related to obligations and costs, are executed in compliance with laws and regulations that could have a direct and material effect on the financial statements, and with any laws and regulations that OMB, DoD, or the IG, DoD, have identified as being significant and for which compliance can be objectively measured and evaluated.

Appendix D includes management and legal representation letters from DeCA.

Internal Control Elements. The purpose of our review of internal controls was not to render an opinion on the financial statements. The three elements of internal controls are the control environment, accounting and related systems, and control procedures. The control environment is the collective effect of various factors on establishing, enhancing, or mitigating the effectiveness of specific policies and procedures. Such factors include management's philosophy and operating style, the entity's organizational structure, and personnel policies and practices. The control environment reflects the overall attitude, awareness, and actions of management concerning the importance of controls and the emphasis placed on them by the entity. Accounting and related systems are the methods and records established to identify, assemble, analyze, classify, record, and report on the entity's transactions and to maintain accountability for the related assets and liabilities. Control procedures are the policies and procedures, in addition to the control environment and the accounting and related systems, that management has established to provide reasonable assurance that specific objectives will be achieved.

Reportable Conditions

Reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of internal controls that, in our judgment, could adversely affect the organization's ability to effectively control and manage its resources and to ensure the preparation of reliable and accurate financial information for use in managing and evaluating operational performance. A material weakness is a reportable condition in which the design or operation of internal controls does not reduce to a relatively low level the risk that errors or irregularities could occur. Such errors or irregularities would be in amounts that would be material to the statements being audited, and would not be detected in a timely manner by employees in the normal course of performing their functions.

Our consideration of internal controls would not necessarily disclose all reportable conditions, and would not necessarily disclose all reportable conditions that are considered to be material weaknesses.

Reportable Condition for DeCA. Internal controls for the FY 1997 Financial Statement of the DeCA Resale Stock Fund were not adequate. Specifically, internal controls for the accounting systems did not provide reasonable assurance that financial information was reliable. Other reportable conditions existed in reconciliation of cash sales, Fund Balance With Treasury, inventory accountability, the recording and reporting of expenses, and reconciliation of deposits.

Management Acknowledgment of Reportable Conditions. The DFAS Annual Statement of Assurance for FY 1997 addressed an uncorrected material control weakness for the Standard Finance System Redesign 1 (SRD-1) disbursing system, which is a subsystem of the Standard Finance System (STANFINS) for generating disbursement data and the Statement of Accountability, Standard Form (SF) 1219. DFAS acknowledged that its SRD-1 disbursing system is deficient because of discrepancies in the reporting of checks issued. Also, DeCA noted in its management representation, "Management Assurance Concerning FY 1997 Defense Commissary Agency Working Capital Fund Financial Statements," February 27, 1998, (Appendix D) that collection information was reported to the Department of the Treasury incorrectly as reverse disbursements.

Accounting Systems. The U.S. Government Standard General Ledger had not been implemented for STANFINS. Also, STANFINS was noncompliant in 5 of the 13 DoD key accounting requirements, including property and inventory accountability and cost accounting. SRD-1 did not have sufficient edit checks to ensure the timely processing of disbursement data, which affected the Fund Balance With Treasury, Accounts Receivable, and Accounts Payable accounts. DFAS does not plan to modify STANFINS and SRD-1 to make them comply with the Chief Financial Officers Act. Instead, DFAS plans to replace STANFINS and SRD-1 with DoD standard systems. The DFAS Indianapolis Center will replace STANFINS with the Defense Joint Accounting System. DFAS plans to include STANFINS in its analysis of alternative systems to support the resale accounting function required by DeCA at the DFAS Columbus Center. DFAS plans to replace the SRD-1 disbursing system with the Defense Standard Disbursement System in November 2000; the system should be fully operational April 2001. The replacement systems should correct the deficiencies noted above. Until STANFINS and SRD-1 are replaced, the ability to produce auditable financial statements will continue to be at risk.

Reconciliation of Cash Sales. Because of several impediments, the Sales Branch, DFAS Columbus Center, was not always able to promptly reconcile unmatched sales and collection transactions reported on the Cash Sales Reconciliation Report, STANFINS AVK-963 Report. Examples of these impediments were electronic media initiatives, such as patron credit and debit cards; discrepancies between store and bank totals; errors in entering data into the Automated System for Army Commissaries and SRD-1; and untimely flow of Reports of Deposit (DD Forms 707) from the DeCA Accounts Control Section to the DFAS Columbus Center.

The AVK-963 Analysis Report, which is a monthly management report manually computed by Sales Branch personnel, identified open line items (items with a net difference between sales and collections) over 30 days old. The report is generated using the AVK-963 Report, which is automatically produced by STANFINS at month's end. The AVK-963 Report is a cumulative report that holds unmatched items until the appropriate sales or collection action is input. The net value of the September 30, 1997, AVK-963 Analysis Report had 3,500 open lines with an actual value of $4.8 million. Of the total net value, $2 million represented unmatched sales and collections over 60 days old (excluding September 1997) that either had not been processed or had been incorrectly posted to STANFINS, through SRD-1. The Disbursing Office may not receive the DD Forms 707 from the Accounts Control Section until 60 days after the original date of the sale, and the collection is not entered into STANFINS through SRD-1 until the funds are received. Also, if the DD Form 707 is received but is not in balance, the collection is not entered until the DD Form 707 is corrected. As a result, the account balances of Sales and Funds Collected as of September 30, 1997, may not have been accurate for financial reporting purposes.

Unmatched Cash Sales and Collections. Cash sales and collections may fail to match because of incorrect document numbers, erroneous posting of sales and collections data, missing DD Forms 707 from commissaries, duplicate debit card transactions using the Point-of-Sale Modernization cash register, and discrepancies between store and bank totals. Unmatched sales or collections items caused by erroneous document numbers or store codes are matched and corrected within the Sales Branch, DFAS Columbus Center, through a "document move." These errors do not directly affect the Sales or Funds Collected account balances. However, the financial reporting of sales and collections is affected by discrepancies between sales and collections caused by bank and store discrepancies, point-of-sale adjustments, deposit or collection adjustments, and missing documentation for DD Forms 707. These discrepancies require corrections to the Sales or Funds Collected general ledger accounts to bring sales and collections into alignment.

Affect on DeCA Financial Reports. Unmatched sales and collections transactions in the AVK-963 Report affect the Sales account balance (general ledger account 5100) and the Funds Collected account balance (general ledger account 1011.1T) in STANFINS. Errors or unmatched items in the "collection" column on the AVK-963 Report, that have been properly researched and reconciled, are reported to the Disbursing Office to correct the STANFINS through SRD-1. Errors or unmatched items in the "sales" column on the AVK-963 Report are reported to the DeCA Analysis and Reconciliation Business Unit to correct STANFINS through the DeCA Interim Business System and the Automated System for Army Commissaries.

Request for Write-Off of Aged Unmatched Transactions. On October 20, 1997, the DFAS Columbus Center, in a memorandum to the Director of Resource Management, DeCA, requested authority to write off a negative amount of $7,690.21 (net). This net amount represents unmatched sales and collections transactions prior to January 1, 1997, largely caused by implementation of the Point-of-Sale Modernization cash register and store and bank total adjustments. DeCA is addressing problems with the implementation of the Point-of Sale Modernization cash register and with balancing store and bank deposit totals.

Fund Balance With Treasury. The SRD-1 disbursement system accepts duplicate transactions involving deposit tickets and debit vouchers. These deficiencies affected the accuracy and timeliness of processing and reconciling financial data for the DeCA Fund Balance With Treasury account (collections and disbursements).

The timely and accurate processing of disbursement data is critical to the Disbursing Office's accountability for the DeCA Resale Stock Fund (Disbursing Station Symbol Number 6355). If the disbursing data are not reconciled within 6 months, the Department of the Treasury charges or credits the amount of the deposit ticket or debit voucher to the Budget Clearing Account, F3878, in the 7th month. As of September 30, 1997, the net balance for F3878 was negative $1 million. Although this amount represents only seven-tenths of 1 percent of the net balance in Fund Balance With Treasury, which is a negative $148.8 million, improvements are needed in reconciling differences between deposits. The DFAS Columbus Center made a request in March 1995 to include edit checks for month and year of transaction and deposit code. See the finding on Reconciliation of Deposits for a discussion of this issue.

Inventory Accountability. According to the DeCA FY 1997 Annual Statement of Assurance, commissary inventory losses increased during FY 1997. DeCA commissaries are required to operate departmental accounts within variances established in DeCA Directive 40-21(C2), "Subsistence Accountability Inventory Procedure," July 15, 1995. At the corporate level, DeCA is required to operate within an established plus or minus percent variance. Overall, DeCA is within the allowable variance. However, within the Continental U.S., DeCA losses for all departments increased from 0.61 percent ($28,215,404) in FY 1996 to 0.72 percent ($31,685,821) in FY 1997. Also, within the Continental U.S., the number of departments outside the allowable tolerance increased from 90 out of 634 in FY 1996 to 110 out of 634 in FY 1997.

Recording and Reporting Expenses. IG, DoD, Report No. 97-223, "Recording and Reporting Expenses of the Defense Commissary Agency," September 30, 1997, stated that expenses of the DeCA Resale Stock Fund were overstated by $15.6 million on the FY 1996 Statement of Operations. This occurred because the DFAS Columbus Center did not properly account for and report discounts earned on purchases. DeCA policy requires that discounts earned on purchases be transferred to the Commissary Surcharge Collections Fund. The DFAS Columbus Center initially recorded discounts in the Cost of Goods Sold - Inventory Gains - Discounts Earned for DeCA Resale. Approximately every 2 weeks, DeCA transferred the amount of the discounts to a suspense account. The Cost of Goods Sold - Inventory Gains - Discounts Earned was then adjusted to a zero balance. Consequently, the Cost of Goods Sold Account for DeCA Resale was not reduced by the amount of discounts earned on purchases.

DFAS initially nonconcurred with the IG, DoD, recommendation to use discounts earned in the calculation of Cost of Goods Sold. However, in subsequent meetings DFAS and the Under Secretary of Defense (Comptroller), Accounting Policy Directorate, have resolved this matter.

Reconciliation of Deposits

The DFAS Columbus Center did not always reconcile deposit differences on the Analysis of Unmatched Transaction Listing for the DeCA Resale Stock Fund in a timely manner. The September 1997 listing (excluding open lines less than 30 days old), identified a net cumulative balance of unmatched deposits totaling $0.7 million. Deposits were not reconciled in a timely manner because the process for reconciling and researching deposit differences was duplicative and ineffective. Although the Directorate of Stock Fund Accounting, DFAS Columbus Center, began taking corrective action, there is a continued risk that deposit differences will not be reconciled before the required reporting date for DoD-wide financial statements. As a result, the financial statements may be inaccurate. In addition, DeCA managers risk overspending or overobligating if they do not have current and accurate information in their Fund Balance With Treasury accounts.

Procedures for Reconciling Deposits

Treasury Financial Manual 2-3100, "Instructions for Disbursing Officers' Reports," April 1, 1997, and DoD 7000.14-R, DoD Financial Management Regulation, volume 5, chapter 5, "Disbursing Policies and Procedures," May 1996, state that the Disbursing Office is responsible for researching and reconciling differences in deposits. Unmatched deposits are the result of differences between deposits recorded by the Department of the Treasury, as reported by the Financial Management Service through the banking system (CA$HLINK), and the deposits recorded by the Disbursing Office, as reported to the Department of the Treasury on the monthly Statement of Accountability, SF 1219. The Department of the Treasury compares the Statement of Accountability with CA$HLINK bank totals for each Disbursing Office and prepares a Statement of Differences-Deposit Transactions (SF 6652). The SF 6652 is forwarded to the DFAS Indianapolis Center monthly. The DFAS Indianapolis Center prepares a monthly Analysis of Unmatched Transaction Listing for DeCA and electronically transmits the differences to the DeCA Accounting Division, DFAS Columbus Center, the following month.

The Analysis of Unmatched Transaction Listing incorporates all unmatched transactions that are currently open (approximately the first six months). Correcting the errors shown on the Analysis of Unmatched Transaction Listing would prevent the Disbursing Office from receiving chargebacks to Budget Clearing Account F3878, from the Department of the Treasury. Chargebacks are unmatched "S" (Statement of Accountability) and "T" (Treasury) lines with voucher dates older than 6 months for amounts less than $5 million. Differences exceeding $5 million remain on the SF 6652 until cleared by the Disbursing Office.

Reconciliation of Deposits

Responsibility for Reconciling Deposits. The assignment of responsibility for reconciling differences in deposits was divided between three functional areas at the DFAS Columbus Center, located in two buildings, and the reconciliation process was not well coordinated between these functional areas. Also, because SRD-1 did not have the necessary edit checks, accounting technicians in the DeCA Reports Control Section, DFAS Columbus Center, were responsible for reentering deposit tickets and debit vouchers into a separate Statement of Accountability database to detect duplicate deposits and debits and erroneous voucher dates entered in SRD-1.

Process for Reconciling Deposits. The process for reconciling deposit differences was duplicative and ineffective and resulted in a negative $1 million (net cumulative) in chargebacks to account F3878. Although that amount represents only seven-tenths of 1 percent of the FY 1997 net account balance for the DeCA Fund Balance With Treasury (negative $148.8 million); according to the Department of the Treasury, the desired balance in account F3878 is zero.

The deposit reconciliation process at the DFAS Columbus Center started in the Disbursing Office. Accounting technicians reconciled the DD Forms 707 (Reports of Deposit), deposit tickets, and debit vouchers, which they received on a daily basis from commissaries, to ensure that the amounts agreed. To detect duplicate deposit and debit entries posted in SRD-1, accounting technicians in the DeCA Reports Control Section, DFAS Columbus Center, reentered the deposits and debits into the Statement of Accountability database. When the documents were in agreement, the technicians input the DD Forms 707 into SRD-1, producing the collection voucher. The collection voucher updated the general ledger account 1011.1T, "Funds Collected," in STANFINS. For deposits and debits that did not agree with CA$HLINK, the technicians researched the differences by requesting documentation from the applicable banks and commissaries.

Deposit differences that were not resolved by the Disbursing Office within 3 months were transferred to financial specialists in the DeCA Reports Analysis Section, DFAS Columbus Center, who were responsible for monitoring the Analysis of Unmatched Transaction Listing. The financial specialists performed further research and resolution of the differences by checking CA$HLINK and contacting the banks and commissaries. Deposit differences that could not be reconciled were charged back to DeCA Resale Stock Fund if outstanding for 6 months. Accounting technicians and financial specialists in the DeCA Reports Analysis Section, who were responsible for monitoring chargebacks, researched and reconciled the chargeback transactions. As of September 30, 1997, the net cumulative balance of unmatched deposits was $121.7 million, including 5,800 October 1997 line items totaling $120.1 million, that were less than 30 days old.

Efforts to Improve the Process for Reconciling Deposits. Effective in March 1998, the DFAS Columbus Center transferred the responsibility for researching and reconciling unmatched differences in deposits and chargeback transactions from the Reports Analysis Section to the Disbursing Office, DFAS Columbus Center. This realignment:

- allows management to develop and implement procedures to improve the work flow and decrease the number of items on the Analysis of Unmatched Transaction Listing,
- centralizes communication among employees involved in the process of reconciling commissary transactions (verifying data through CA$HLINK and contacting banks and commissaries), and
- assists management in identifying problem areas and determining the most effective means of eliminating items on the Analysis of Unmatched Transaction Listing.

DFAS Columbus Center's Audit of the Deposit Reconciliation Process. The Office of Internal Review, DFAS Columbus Center, issued Report No. 97-A-670-UA-003, "The DFAS-Wide Audit of the Disbursing Office Deposit Reconciliation Process," on January 28, 1998. The auditors reported that more aggressive action was needed to clear deposits-in-transit to prevent deposits from being charged back to account F3878. The Office of Internal Review recommended that the DFAS Columbus Center establish a goal of eliminating all chargebacks to account F3878 and perform a trend analysis of commissary records of deposits-in-transit to identify at least five commissaries that have a large number of chargebacks. Management agreed to establish a goal of eliminating chargebacks, but preferred to delay identifying the five commissaries until a Pareto analysis[1] is completed.

Further Improvements Needed. Although transferring the responsibility of unmatched and chargeback deposits will minimize duplication of effort and make the reconciliation process more efficient, further improvements are needed. Specifically, DeCA needs to improve its procedures for forwarding deposit and debit information to the DFAS Columbus Center to ensure the timely and accurate posting of disbursement data to SRD-1. Timely and accurate disbursement data are critical to the Disbursing Office's accountability for the DeCA Resale Stock Fund, as reported on the monthly Statement of Accountability, SF 1219. Managers risk overspending or overobligating if they do not have current and accurate information on their Fund Balance With Treasury accounts, which are reported on the SF 1219.

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[1]The Pareto Method of Quality Improvement involves determining the source or sources and cause or causes that create a major part of the quality program. Experience has shown that, in many instances, a relatively small percentage (20 percent) of persons or machines or sources accounts for a large percentage (80 percent) of the quality problem.

Also, when studying alternative accounting systems for the DeCA Resale Stock Fund business area, Headquarters, DFAS, should consider a system that is compatible with the Defense Standard Disbursing System and the Defense Joint Accounting System. This will minimize problems between the systems and improve the deposit reconciliation process.

Conclusion

Until DFAS Columbus Center remedies the lack of edit checks in SRD-1, differences in deposits may not be reconciled before the required reporting date for the DoD-wide financial statements. The Defense Standard Disbursing System, which is scheduled for implementation in November 2000 through April 2001, should correct the deficiencies in SRD-1. Until the new system is implemented, the Reports Control Section, DFAS Columbus Center, plans to continue entering into the Statement of Accountability database the deposit tickets and debit vouchers that the Disbursing Office has processed in SRD-1, in order to detect duplicate entries and erroneous transaction dates.

DeCA procedures for forwarding deposit and debit information to the DFAS Columbus Center need to be clarified and standardized to minimize differences in deposits and expedite the reconciliation of deposits.

Recommendations and Requirements for Management Comments

1. We recommend that the Director, Defense Finance and Accounting Service, consider, in studying alternative accounting systems for the Defense Commissary Agency Resale Stock Fund, a system that is compatible with the Defense Standard Disbursing System and the Defense Joint Accounting System.

Management Comments Required. The Director, Defense Finance and Accounting Service, did not comment on a draft of this report. We request the Director provide comments on this report.

2. We recommend that the Director, Defense Commissary Agency, clarify and standardize procedures related to forwarding deposit and debit information to the Defense Finance and Accounting Service Columbus Center in order to expedite the reconciliation of deposits between commissaries and the Defense Finance and Accounting Service Columbus Center.

Management Comments. The Director, Defense Commissary Agency, concurred and will clarify procedures related to forwarding deposit and debit information in the Defense Commissary Agency Directive 70-6. The target date for revising the directive is September 30, 1998.

Part I. B. - Review of Compliance With Laws and Regulations

Introduction

We audited the DeCA Resale Stock Fund Financial Statements for material instances of noncompliance with laws and regulations for FY 1997. Our objective was to assess compliance with laws and regulations for transactions and events that could have a direct and material effect on the DeCA Resale Stock Fund Financial Statements. Such tests are required by the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994. We reviewed compliance with laws and regulations, not to render an opinion on overall compliance with such provisions, but to obtain reasonable assurance that the financial statements were free of material misstatements. Since DeCA was established on October 1, 1991, the agency has made improvements in documenting its policies and procedures. See Appendix E for a list of the laws and regulations we reviewed.

Reportable Noncompliances

Material instances of noncompliance are failures to follow requirements, laws, or regulations that would cause us to conclude that the aggregation of the misstatements resulting from those failures is either material to the financial statements, or that the sensitivity of the matter would cause others to perceive it as significant.

Title 31, U.S. Code (U.S.C.) 501, "Chief Financial Officers Act of 1990." The Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, requires DoD to prepare agency-wide audited financial statements and submit them to OMB no later than March 1, 1998. DoD did not prepare and issue financial statements for FY 1997 in time for the auditors to render an opinion on the financial statements. The statements were late and unauditable primarily because DoD had inadequate accounting systems and control procedures. The untimely preparation of the DeCA FY 1997 Financial Statements and deficiencies in accounting systems and control procedures were reasons we were unable to render an opinion on those financial statements. Those deficiencies prevented DeCA from completely and accurately disclosing timely financial results; obtaining the financial information needed for managing; and using accounting results to prepare and support budget requests and control its budget.

Title 31, U.S.C. 3512, "Federal Financial Management Improvement Act of 1996." On September 9, 1997, OMB issued a memorandum, "Implementation Guidance for the Federal Financial Management Improvement Act (FFMIA) of 1996." The Federal Financial Management Improvement Act requires Federal agencies to implement and maintain financial management systems that comply substantially with Federal requirements for financial management systems, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level. The Federal Financial Management Improvement Act also requires that the IG, DoD, report on agency compliance with Federal requirements and accounting standards, and the U.S. Government Standard General Ledger. These requirements are established in the following documents.

- OMB Circular No. A-127, "Financial Management Systems," July 23, 1993, establishes Government policy for developing, evaluating, and reporting on financial management systems. It requires financial management systems to provide complete, reliable, consistent, timely, and useful information. To achieve this goal, DoD and other Federal agencies must establish and maintain a single, integrated financial management system that uses the U.S. Government Standard General Ledger. DoD financial management systems did not comply with the requirements of OMB Circular No. A-127. DoD used multiple, nonintegrated financial systems that did not contain the U.S. Government Standard General Ledger. Although DoD had its own general ledger, that ledger did not control all financial transactions and balances and was not the only source of information for financial reports.

- OMB Circular No. A-134, "Financial Accounting Principles and Standards," May 20, 1993, establishes policies and procedures for approving and publishing financial accounting principles and standards. It also establishes the policies that Executive agencies and OMB are to follow in seeking and providing interpretations and other advice related to the standards.

- Joint Financial Management Improvement Program Federal Financial Management System Requirements is a cooperative undertaking of the OMB, the Department of the Treasury, and the Office of Personnel Management, working with each other and with Federal agencies to improve financial management practices throughout the Government. The Joint Financial Management Improvement Program has published a series of "Federal Financial Management System Requirements."

- The "Core Financial System Requirements," September 1995, which are part of the Joint Financial Management Improvement Program's "Federal Financial Management System Requirements," establish standard requirements for the foundation modules of an agency's integrated financial management system. These requirements state that a financial management system must support the partnership between program and financial managers and assure the integrity of information for decision making and performance measures.

As part of our audit to obtain reasonable assurance about whether the FY 1997 DeCA Financial Statements were free of material misstatement, we performed limited tests of their compliance with certain provisions of laws and regulations when noncompliance could have a direct and material effect on the determination of amounts in the financial statements. We also tested compliance with certain other laws and regulations specified in OMB Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993, modified by OMB Bulletin No. 98-04, "Addendum to OMB Bulletin No. 93-06," January 16, 1998. In planning and performing our tests of compliance, we considered the implementation guidance issued by OMB on September 9, 1997, relating to the Federal Financial Management Improvement Act.

The financial management systems that support the FY 1997 DeCA Financial Statements of the DeCA Resale Stock Fund were not in substantial compliance with the requirements of the Federal Financial Management Improvement Act. The DoD financial management systems comprise multiple finance, accounting, and feeder systems that are the responsibility of DFAS and DeCA. DFAS financial management systems were unable to produce auditable and timely financial statements for FY 1997 primarily because the accounting and related systems were not designed for financial reporting. The financial condition of DeCA and its operating results for FY 1997 were not verifiable, and DeCA had no assurance that it was properly managing its resources.

Reportable Noncompliance. Accounting systems and internal controls did not completely or accurately disclose the financial condition of DeCA, as required by 31 U.S.C. Under the "Federal Financial Management Improvement Act of 1996" and OMB Bulletin No. 98-04. The financial management systems did not comply with Federal requirements for financial management systems (OMB Circular No. A-127) and the U.S. Government Standard General Ledger at the transaction level.

The financial management systems that supported the FY 1997 Financial Statements of the DeCA Resale Stock Fund, were not in compliance with the requirements of the "Federal Financial Management Improvement Act of 1996" or OMB Circular No. A-127, "Financial Management Systems," July 23, 1993. DFAS financial management systems were unable to produce auditable financial statements for FY 1997. According to the System Manager/User Review Certification Statement for FYs 1997 and 1996, STANFINS is noncompliant in 5 of the 13 DoD key accounting requirements, including system controls, property and inventory accountability, and cost accounting.

The DeCA management representation, "Management Assurance Concerning FY 1997 Defense Commissary Agency Working Capital Fund Financial Statements," February 27, 1998, stated that collection information was reported to the Department of the Treasury incorrectly as reverse disbursements. The DFAS Columbus Center submitted unsupported monthly adjustments to the Department of the Treasury through the Data Element Management/Accounting Reporting System, and $30 million in undistributed disbursements was transferred from the Defense Working Capital Fund Corporate account to the Fund Balance With Treasury account. As a result, the Fund Balance With Treasury account could not be validated.

The SRD-1 disbursement system accepted duplicate deposit and debit transactions. To prevent duplicate transactions, the SRD-1 system required edit checks to verify the month and year of transaction and the deposit code. These deficiencies affected the accuracy and timeliness of processing and reconciling financial data on collections and disbursements for the DeCA Fund Balance With Treasury account. The finding in Part I.A. discusses deficiencies in SRD-1.

DFAS, the preparer of the DeCA financial statements, continued to be in noncompliance with regulations. The DFAS Columbus Center reported Accounts Payable for the DeCA Resale Stock Fund at the gross amount, excluding purchase discounts. The DoD Regulation 7000.14-R, volume 4; "Accounting Policy and Procedures," chapter 9, "Accounts Payable," January 1995, requires that Accounts Payable be reported net of all purchase discounts. The DFAS Columbus Center did not report Accounts Payable in accordance with DoD guidance. Consequently, the DeCA Resale Stock Fund Accounts Payable for FY 1997 was overstated by $17.8 million, which was the amount of the purchase discounts earned for FY 1997.

DFAS did not promptly reconcile deposit differences shown on the Statement of Differences issued by the Department of the Treasury. Consequently, the Fund Balance With Treasury will be misstated. For more details, see the finding on deposit reconciliations in Part I. A.

Part II - Additional Information

Appendix A. Audit Process

Scope

Statements Reviewed. We performed a limited review of the FY 1997 Financial Statements of the DeCA Resale Stock Fund. The statements consisted of the Statement of Financial Position, the Statement of Operations and Changes in Net Position, the Statement of Cash Flows, and accompanying footnotes. We did not review the Statement of Cash Flows. Also, in FY 1996, DeCA was included in the Defense Business Operations Fund Consolidated Financial Statements; therefore, we did not examine the FY 1996 portion of the DeCA Resale Stock Fund Comparative Financial Statements. The final versions of the DeCA financial statements were submitted to us on February 6, 1998.

To fulfill our responsibility to render an opinion on the FY 1997 Financial Statements of the DeCA Resale Stock Fund, we coordinated our audit efforts with DeCA and DFAS.

Scope Limitations. We did not audit the FY 1996 financial data reported on the DeCA Consolidated Financial Statements for FYs 1997 and 1996. The DeCA Consolidated Financial Statements consisted of statements for DeCA Operations and the DeCA Resale Stock Fund. We did not audit the financial statements for DeCA Operations. In addition, we did not receive the financial statements in a timely manner; therefore, we could not determine the accuracy and completeness of the data reported. Also, we were unable to observe a physical inventory at any commissary because the inventories were completed before we began audit work; inventory is 76 percent of the DeCA Resale Stock Fund's total assets. Further, our review was limited to 4 out of 299 commissaries.

Accounting Principles. Accounting principles and standards for the Federal Government are under development. The Federal Accounting Standards Advisory Board was established to recommend Federal accounting standards to three officials for approval. Those three officials are the Director, OMB; the Secretary of the Treasury; and the Comptroller General. The Director, OMB, and the Comptroller General of the U.S. issue standards agreed on by the three officials. To date, seven accounting standards and two accounting concepts have been published in final form. Accounting Standard No. 8 has been approved by the Federal Accounting Standards Advisory Board, but it must be reviewed by Congress before it is issued. In addition, the Federal Accounting Standards Advisory Board issued an exposure draft, "Amendments to Accounting for Property, Plant, and Equipment," February 13, 1998, proposing amendments to Standards No. 6 and No. 8. These standards and concepts constitute generally accepted accounting principles for the Federal government. OMB Bulletin No. 94-01, as amended by OMB Bulletin No. 97-01, incorporates these standards and concepts and should be used by Federal agencies to prepare their financial statements. The following table lists the "Statements of Federal Financial Accounting Standards and Concepts."

Statements of Federal Financial Accounting Standards and Concepts

Accounting Standards and Concepts	Title	Status	Fiscal Year Effective
Standard No. 1	Accounting for Selected Assets and Liabilities, March 30, 1993	Final	1994
Standard No. 2	Accounting for Direct Loans and Loan Guarantees, August 23, 1993	Final	1994
Standard No. 3	Accounting for Inventory and Related Property, October 27, 1993	Final	1994
Standard No. 4	Managerial Cost Accounting Concepts and Standards, July 31, 1995	Final	1998
Standard No. 5	Accounting for Liabilities of the Federal Government, December 20, 1995	Final	1997
Standard No. 6	Accounting for Property, Plant, and Equipment, November 30, 1995	Final*	1998
Standard No. 7	Accounting for Revenue and Other Financing Sources, May 10, 1996	Final	1998
Standard No. 8	Supplementary Stewardship Reporting, June 11, 1996	Approved*	
Concept No. 1	Objectives of Federal Financial Reporting, September 2, 1993	Final	
Concept No. 2	Entity and Display, June 6, 1995	Final	

*FASAB issued an exposure draft, "Amendments to Accounting for Property, Plant, and Equipment," on February 13, 1998. The exposure draft contains proposed amendments to Standards No. 6 and No. 8.

Through FY 1997, agencies were required to follow the hierarchy of accounting principles outlined in OMB Bulletin No. 94-01, as amended by OMB Bulletin No. 97-01. A summary of the FY 1997 hierarchy follows:

- standards agreed to and published by the Director, OMB; the Secretary of the Treasury; and the Comptroller General of the U.S.;
- requirements for form and content in OMB Bulletin No. 94-01, as amended by OMB Bulletin No. 97-01;

- accounting standards in agency accounting policy, procedures, or other guidance as of March 29, 1991; and
- accounting principles published by other authoritative sources.

Review of Internal Controls. Our consideration of the internal controls included obtaining an understanding of significant internal control policies and procedures and assessing the level of control risk relevant to all significant cycles, classes of transactions, or account balances. For the control policies and procedures that had been properly designed and placed in operation, we performed sufficient tests to provide reasonable assurance that the controls were effective and working as designed. For controls that were determined to be weak, we attempted to perform tests to determine the level of assurance that could be placed on those controls.

Our consideration of the internal controls would not necessarily disclose all matters that are reportable conditions, and would not necessarily disclose all reportable conditions that are also considered to be material weaknesses.

Review of Compliance With Laws and Regulations. As part of obtaining reasonable assurance about whether the DeCA Financial Statements for FYs 1997 and 1996 were free of material misstatements, we reviewed compliance with laws and regulations that may directly affect the financial statements, and other laws and regulations designated by the OMB and the DoD. Appendix E lists the laws and regulations we reviewed.

Methodology

Auditing Standards. We conducted our financial statement audit in accordance with generally accepted Government auditing standards issued by the Comptroller General of the U.S., as implemented by the IG, DoD, and OMB Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. We relied on the guidelines suggested by the General Accounting Office and our professional judgment in assessing the materiality of matters affecting the fair presentation of the financial statements and related internal control weaknesses.

Computer-Processed Data. To achieve the overall audit objectives, we relied on computer-processed data in the DeCA feeder systems[2] and the DFAS

[2] DeCA feeder systems include the DeCA Interim Business System, the Automated System for Army Commissaries, and the Standard Automated Voucher Examination System. The Interim Business System accounts for such things as commissary receipts and sales, the Automated System for Army Commissaries provides inventory control for commissaries and the Voucher Examination System is DeCA's bill paying system. These feeder systems interface with STANFINS for financial reporting purposes.

STANFINS and SRD-1 systems. We assessed the reliability of these data by evaluating the internal controls designed to properly record, process, and summarize transactions in the DeCA systems and the STANFINS general ledger. We focused on tracing transactions from input through entry into the STANFINS general ledger. The information provided by those systems was generally reliable, and the discrepancies identified were not material to the financial statements.

Audit Assistance. We reviewed Report No. 97-A-670-UA-003, "DFAS-Wide Audit of the Disbursing Office Deposit Reconciliation Process for the Columbus Center," issued by the Office of Internal Review, DFAS Columbus Center, on January 28, 1998. We used their audit work specific to unmatched and chargeback procedures and processes for the Reports Analysis Section, Reports Control Section, and the Disbursing Office, DFAS Columbus Center.

Audit Period and Locations. The audit was conducted from August 1997 to April 1998 at various offices of the DFAS and DeCA.

Representation Letter. We received a management representation letter from the Chief Financial Officer, DeCA, dated February 27, 1998, regarding the DeCA FY 1997 Financial Statements. The letter cited problems in the accuracy of various account balances provided by and used by DFAS to prepare the financial statements. We also received a legal representation letter dated February 27, 1998. See Appendix D for the management and legal representation letters.

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

Management Control Program

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

Scope of Review. We performed a review of management controls over the preparation of the FY 1997 Financial Statements of the DeCA Resale Stock Fund. We reviewed controls over the recording, processing, and summarizing of revenue, inventory, and accounts payable transactions in the STANFINS general ledger and the recording and posting of collection and disbursement data through SRD-1, which interfaces with STANFINS. We also reviewed management's self-evaluation of the controls.

Adequacy of Management Controls. We identified material management control weaknesses, as defined by DoD Directive 5010.38, in the preparation of the FY 1997 Financial Statements of the DeCA Resale Stock Fund. The STANFINS and SRD-1 accounting systems did not provide reasonable assurance that financial information was reliable. STANFINS had not implemented the U.S. Government Standard General Ledger and was noncompliant in 5 of the 13 key accounting requirements for DoD. The SRD-1 did not have sufficient edit checks to ensure the timely processing of disbursement data that may affect the Fund Balance With Treasury, Accounts Receivable, and Accounts Payable accounts. Additionally, STANFINS did not meet the requirements of the Federal Financial Management Improvement Act of 1996 or OMB Circular No. A-127. DFAS plans to replace STANFINS and SRD-1 with DoD standard systems. These replacement systems should correct the weaknesses noted above. As a result, we have not made recommendations regarding these weaknesses. Correction of the weaknesses noted above should improve the reliability of financial information. A copy of the report will be provided to the senior official responsible for management controls at DFAS.

Adequacy of Management Self-Evaluation. The DFAS Annual Statement of Assurance for FY 1997 addressed an uncorrected material control weakness for the SRD-1 disbursing system, which is a subsystem of STANFINS that generates disbursement data and the SF 1219. The DFAS acknowledged that its SRD-1 disbursing system is deficient because of discrepancies in the reporting of checks issued. The Department of the Treasury has reported discrepancies between checks issued from SRD-1, as reported by Disbursing Offices on the Month-End Check Issue Summary (SF 1179), and the monthly summary of checks issued, as reported on the SF 1219. When these reports do not agree, either the overall liability for outstanding checks or the agency's account is misstated.

DFAS did not identify the lack of edit checks in SRD-1 as a material internal control weakness, although that deficiency creates the risk that differences in deposits will not be reconciled before the required reporting date for DoD-wide financial statements. Furthermore, DFAS did not identify material internal control weaknesses for its STANFINS accounting system, although STANFINS was deficient in 5 of the 13 key accounting requirements for DoD. However, the DoD Annual Statement of Assurance for FY 1997 stated that DoD financial information was not always maintained adequately by accounting systems, was not fully compliant with regulatory and statutory requirements, and could not be used to prepare auditable financial statements.

We consider the deficiencies in STANFINS and SRD-1 to be material internal control weaknesses because the financial information those systems generate cannot be used to produce reliable financial reports.

Appendix B. Prior Audit Reports

Inspector General, DoD

Report No. 97-223, "Recording and Reporting Expenses of the Defense Commissary Agency," September 30, 1997. The report states that some expenses were not properly recorded and reported because DFAS Columbus Center personnel did not follow DoD guidance in accounting for discounts earned on purchases of goods acquired for resale. As a result, the expenses of the DeCA Resale Stock Fund were overstated by $15.6 million on the FY 1996 Statement of Operations. Although this weakness was not material to the financial statements, correcting the weakness will improve the accuracy of the statements. The report recommended that the DFAS Columbus Center accumulate discounts earned on purchases in the general ledger account Cost of Goods Sold-Inventory Gains-Discounts Earned, and include them in calculating the cost of goods sold. DFAS and the Under Secretary of Defense (Comptroller), Accounting Policy Directorate, initiated action to resolve this issue.

Report No. 95-228, "Statement of Financial Position for the Commissary Resale Stock Fund, as of September 30, 1994," June 8, 1995. The report states that the internal control structure over transaction processing and general ledger recordings in the DeCA Resale Stock Fund did not provide reasonable assurance of an accurate inventory balance. As a result, the inventory balance of $574.7 million, reported on the Statement of Financial Position, reflected loss adjustments of $55.4 million, and DeCA could not determine the amount of the misstatement as of September 30, 1994; therefore, the amount could be materially misstated. The report also states that the internal controls over transaction processing and general ledger recording in the DeCA Resale Stock Fund did not provide reasonable assurance of an accurate balance in Accounts Payable-Transactions With Federal Entities. As a result, the balance of Accounts Payable-Transactions With Federal Entities reported at $166 million on the Statement of Financial Position reported as of September 30, 1994, could be materially misstated. The report recommended that DeCA implement followup procedures to ensure that stores receive transferred merchandise and that supporting documentation is maintained. The report also recommended that DeCA implement controls over entering merchandise receipts into the computer system, over the regional review and approval of internal control checklists, and over the preparation of timely, effective reports of survey by independent personnel. The report recommended that DeCA adhere to the DoD Accounting Manual by directing that the Accounts Payable-Transactions with Federal Entities general ledger account be reconciled with the documentation for vouchers. Management generally concurred with the report.

Report No. 94-184, "Controls Over Management of Meat and Tobacco Products at Selected Commissary Stores," September 6, 1994. The report states that DeCA did not have effective management controls over inventories of meat and tobacco products. The stores did not require periodic counts of tobacco products or other high-value inventory to be compared to accounting and inventory records. They also did not implement existing internal controls for the segregation of duties, maintenance of accounting documentation, use of automated meat cutting test, and physical security. As a result, financial records were unreliable. The report recommended that DeCA revise directives to require its stores to compare monthly physical inventories of meat to the balances shown in automated systems. DeCA partially concurred, and later stated that system modifications would be needed to reconcile the results of the monthly meat inventory to data in the automated systems.

The report also recommended that DeCA revise its procedures to require stores to count tobacco and other high-value inventory items on a monthly basis and compare these counts to data in the automated systems. DeCA was acquiring a new business system and a new Point-of-Sale system that could account for tobacco products as a separate entity. The corrective actions satisfied the intent of the recommendation.

Finally, the report recommended that DeCA require its regional managers to monitor compliance with internal controls and establish plans to train personnel at management support centers in DeCA accounting policies and procedures. DeCA emphasized the requirement for the regions to monitor store activities to ensure compliance with procedures. DeCA has also formed management assistance teams for all phases of operations, including the training of personnel at management support centers. The corrective actions satisfied the intent of the recommendations.

Report No. 94-183, "Commissary Revenues," September 6, 1994. The report states that DeCA did not adequately safeguard and account for cash receipts. The report recommended that DeCA establish controls for proper authorization of voids and refunds, collection of cash receipts from registers, deposits, physical security, security escorts, preparation of deposit reports, tracking of dishonored checks, segregation of duties for cash receipt, and prompt reconciliation by service centers of store sales and deposits. Management initiated corrective actions.

Report No. 94-157, "Defense Commissary Agency Financial Management Improvement Program," June 30, 1994. The report states that DeCA had made significant improvements in six functional areas of its Financial Management Improvement Program: accrued expenses, automated data processing, contract payments, fixed assets, inventory, and sales and deposits. The audit disclosed no material deficiencies in implementing the DeCA Financial Management Improvement Program. Management concurred with the report.

Report No. 93-147, "Defense Commissary Resale Stock Fund Financial Statements for FY 1992," June 30, 1993. The report states that the auditors identified material internal control weaknesses over vendor payments and inventory accountability. Additionally, DeCA had not documented many of its operating and accounting policies and procedures. The report concluded that the financial statements and the Notes to the Financial Statements did not present fairly the financial portion of the fund.

Report No. 93-124, "Defense Commissary Agency Vendor Payments, Returned Checks, and Rebates," June 24, 1993. This report states that during the first half of FY 1992, DeCA did not adequately control financial transactions for vendor payments, returned checks, and rebates. As a result, DeCA could not be assured that the financial accounts for vendor payments represented appropriately authorized transactions, and the DeCA financial statements could be misstated. The report recommended that DeCA issue or modify procedures to ensure that the receipt of vendor merchandise is verified, contracting officers receive prompt feedback when fast payment vendors are deficient, and that checks from vendors are endorsed and deposited promptly. Management generally concurred with the report.

Report No. 93-096, "The System Used by the Defense Commissary Agency to Pay Vendors' Invoices," May 14, 1993. The report states that the DeCA system for paying vendors' invoices was not timely. As a result, DeCA missed savings available through vendor discounts and incurred unnecessary interest costs. The report recommended that the Director, DeCA, require service centers and commissaries to improve the bill-paying process, taking maximum advantage of discounts for prompt payments and minimizing interest costs. Management concurred with the recommendations and stated that procedures were being established to pay invoices promptly.

Appendix C. Principal Statements and Footnotes

This appendix (a total of 28 pages) consists of the DeCA Working Capital Fund Consolidated Principal Statements and accompanying footnotes. A complete set of the DeCA Working Capital Fund Financial Statements is available at the following web site address:

http://www.DTIC.MIL/Comptroller/FMFIA.html.

DEFENSE COMMISSARY AGENCY

WORKING CAPITAL FUND

CONSOLIDATED PRINCIPAL STATEMENTS

Department of Defense
Defense Commissary Agency - Working Capital Fund - Consolidated
Statement of Financial Position
As of September 30, 1997
(Thousands)

ASSETS	1997	1996
1. Entity Assets:		
a. Transactions with Federal (Intragovernmental) Entities:		
(1) Fund Balance with Treasury (Note 2)	($196,813)	($307,990)
(2) Investments, Net (Note 4)	0	0
(3) Accounts Receivable, Net (Note 5)	7,230	14,376
(4) Interest Receivable	0	0
(5) Advances and Prepayments	0	0
(6) Other Federal (Intragovernmental) (Note 6)	0	0
b. Transactions with Non-Federal (Governmental) Entities:		
(1) Investments (Note 4)	0	0
(2) Accounts Receivable, Net (Note 5)	148,751	56,070
(3) Credit Program Receivables/ Related Foreclosed Property, Net (Note 7)	0	0
(4) Interest Receivable, Net	0	0
(5) Advances and Prepayments	1,194	934
(6) Other Non-Federal (Governmental) (Note 6)	0	0
c. Cash and Other Monetary Assets (Note 3)	0	0
d. Inventory, Net (Note 8)	328,035	347,019
e. Work in Process (Note 9)	0	0
f. Operating Materials/Supplies, Net (Note 10)	0	0
g. Stockpile Materials, Net (Note 11)	0	0
h. Seized Property (Note 12)	0	0
i. Forfeited Property, Net (Note 13)	0	0
j. Goods Held Under Price Support and Stabilization Programs, Net (Note 14)	0	0
k. Property, Plant and Equipment, Net (Note 15)	533	439
l. War Reserves	0	0
m. Other Entity Assets	99,154	154,535
n. Total Entity Assets	$388,084	$265,383
2. Non-Entity Assets:		
a. Transactions with Federal (Intragovernmental) Entities:		
(1) Fund Balance with Treasury (Note 2)	$0	$0
(2) Accounts Receivable, Net (Note 5)	0	0
(3) Interest Receivable, Net	0	0
(4) Other (Note 6)	0	0

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Commissary Agency - Working Capital Fund - Consolidated
Statement of Financial Position
As of September 30, 1997
(Thousands)

ASSETS, Continued	1997	1996
2. Non-Entity Assets:		
b. Transactions with Non-Federal (Governmental) Entities:		
(1) Accounts Receivable, Net (Note 5)	$0	$0
(2) Interest Receivable, Net	0	0
(3) Other (Note 6)	0	0
c. Cash and Other Monetary Assets (Note 3)	0	0
d. Other Non-Entity Assets	0	0
e. **Total Non-Entity Assets**	$0	$0
3. Total Assets	$388,084	$265,383
LIABILITIES		
4. Liabilities Covered by Budgetary Resources:		
a. Transactions with Federal (Intragovernmental) Entities:		
(1) Accounts Payable	$171,645	$260,520
(2) Interest Payable	0	0
(3) Debt (Note 16)	0	0
(4) Other Federal (Intragovernmental) Liabilities (Note 17)	0	0
b. Transactions with Non-Federal (Governmental) Entities:		
(1) Accounts Payable	431,228	431,065
(2) Accrued Payroll and Benefits		
(a) Salaries and Wages	13,682	14,928
(b) Annual Accrued Leave	0	0
(c) Severance Pay and Separation Allowance	0	0
(3) Interest Payable	0	0
(4) Liabilities for Loan Guarantees (Note 7)	0	0
(5) Lease Liabilities (Note 18)	0	0
(6) Pensions and Other Actuarial Liabilities (Note 19)	0	0
(7) Other Non-Federal (Governmental) Liabilities (Note 17)	0	0
c. **Total Liabilities Covered by Budgetary Resources:**	$616,555	$706,513

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Commissary Agency - Working Capital Fund - Consolidated
Statement of Financial Position
As of September 30, 1997
(Thousands)

LIABILITIES, Continued	1997	1996
5. Liabilities Not Covered by Budgetary Resources:		
a. Transactions with Federal (Intragovernmental) Entities:		
(1) Accounts Payable	$0	$0
(2) Debt (Note 16)	0	0
(3) Other Federal (Intragovernmental) Liabilities (Note 17)	0	0
b. Transactions with Non-Federal (Governmental) Entities:		
(1) Accounts Payable	0	0
(2) Debt (Note 16)	0	0
(3) Lease Liabilities (Note 18)	0	0
(4) Pensions and Other Actuarial Liabilities (Note 19)	64,945	0
(5) Other Non-Federal (Governmental) Liabilities (Note 17)	30,365	28,211
c. Total Liabilities Not Covered by Budgetary Resources	$95,310	$28,211
6. Total Liabilities	$711,865	$734,724
NET POSITION (Note 20)		
7. Balances:		
a. Unexpended Appropriations (Note 31C)	$66,666	$56,442
b. Invested Capital	5,168,537	3,822,955
c. Cumulative Results of Operations	(5,463,674)	(4,320,527)
d. Other	0	0
e. Future Funding Requirements	(95,310)	(28,211)
f. Total Net Position	($323,781)	($469,341)
8. Total Liabilities and Net Position	$388,084	$265,383

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Commissary Agency - Working Capital Fund - Consolidated
Statement of Operations and Changes in Net Position
For the Period Ended September 30, 1997
(Thousands)

	1997	1996
REVENUES AND FINANCING SOURCES		
1. Appropriated Capital Used (Note 31C)	$906,214	$822,258
2. Revenues from Sales of Goods and Services		
a. To the Public	5,134,642	5,236,286
b. Intragovernmental	34,906	47,147
3. Interest and Penalties, Non-Federal	0	0
4. Interest, Federal	0	0
5. Taxes (Note 21)	0	0
6. Other Revenues and Financing Sources (Note 22)	58,937	1,583
7. Less: Taxes and Receipts Transferred to the Treasury or Other Agencies	0	0
8. Total Revenues and Financing Sources	$6,134,699	$6,107,274
EXPENSES		
9. Program or Operating Expenses (Note 23)	$970,144	$981,520
10. Cost of Goods Sold (Note 24)		
a. To the Public	5,141,668	5,296,086
b. Intragovernmental	27,389	42,109
11. Depreciation and Amortization	30	355
12. Bad Debts and Writeoffs	6,343	232
13. Interest		
a. Federal Financing Bank/Treasury Borrowing	0	0
b. Federal Securities	0	0
c. Other	530	398
14. Other Expenses (Note 25)	58,651	322
15. Total Expenses	$6,204,755	$6,321,022
16. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses Before Extraordinary Items	($70,056)	($213,748)
17. Plus (Minus) Extraordinary Items (Note 26)	0	0
18. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	($70,056)	($213,748)

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Commissary Agency - Working Capital Fund - Consolidated
Statement of Operations and Changes in Net Position
For the Period Ended September 30, 1997
(Thousands)

	1997	1996
EXPENSES, Continued		
19. Net Position, Beginning Balance, as Previously Stated	($469,341)	($808,093)
20. Adjustments (Note 27)	(250,833)	(47)
21. Net Position, Beginning Balance, as Restated	($720,174)	($808,140)
22. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	(70,056)	(213,748)
23. Plus (Minus) Non Operating Changes (Note 28)	466,449	552,547
24. Net Position, Ending Balance	($323,781)	($469,341)

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Commissary Agency - Working Capital Fund - Consolidated
Statement of Cash Flows
For the Period Ended September 30, 1997
(Thousands)

	1997	1996
CASH FLOWS FROM OPERATING ACTIVITIES		
1. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	($70,056)	($213,748)
Adjustments Affecting Cash Flow:		
2. Appropriated Capital Used (Note 31C)	(906,214)	(822,258)
3. Decrease (Increase) in Accounts Receivable	(85,536)	57,577
4. Decrease (Increase) in Other Assets	18,655	65,172
5. Increase (Decrease) in Accounts Payable	(88,917)	(277,291)
6. Increase (Decrease) in Other Liabilities	(1,246)	3,313
7. Depreciation and Amortization	30	355
8. Other Unfunded Expenses	0	0
9. Other Adjustments	(251,064)	190
10. Total Adjustments	($1,314,292)	($972,942)
11. Net Cash Provided (Used) by Operating Activities	($1,384,348)	($1,186,690)
CASH FLOWS FROM INVESTING ACTIVITIES		
12. Sale of Property, Plant and Equipment	$0	$0
13. Purchase of Property, Plant and Equipment	0	0
14. Sale of Securities	0	0
15. Purchase of Securities	0	0
16. Collection of Loans Receivable	0	0
17. Creation of Loans Receivable	0	0
18. Other Investing Cash Provided (Used)	0	0
19. Net Cash Provided (Used) by Investing Activities	$0	$0
CASH FLOWS FROM FINANCING ACTIVITIES		
20. Appropriations (Current Warrants)	$916,438	$878,700
21. Add:		
a. Restorations	0	0
b. Transfers of Cash from Others	271,097	0
22. Deduct:		
a. Withdrawals	0	0
b. Transfers of Cash to Others	(307,990)	(533,193)
23. Net Appropriations	$1,495,525	$1,411,893

The accompanying notes are an integral part of these statements.

Department of Defense
Defense Commissary Agency - Working Capital Fund - Consolidated
Statement of Cash Flows
For the Period Ended September 30, 1997
(Thousands)

	1997	1996
CASH FLOWS FROM FINANCING ACTIVITIES, Continued		
24. Borrowing from the Public	$0	$0
25. Repayments on Loans to the Public	0	0
26. Borrowing from the Treasury and the Federal Financing Bank	0	0
27. Repayments on Loans from the Treasury and the Federal Financing Bank	0	0
28. Other Borrowings and Repayments	0	0
29. Net Cash Provided (Used) by Financing Activities	$1,495,525	$1,411,893
30. Net Cash Provided (Used) by Operating, Investing and Financing Activities	$111,177	$225,203
31. Fund Balance with Treasury, Cash, and Foreign Currency, Beginning	(307,990)	(533,193)
32. Fund Balance with Treasury, Cash, and Foreign Currency, Ending	($196,813)	($307,990)

Supplemental Disclosure of Cash Flow Information:	1997	1996
33. Total Interest Paid	$530	$398

Supplemental Schedule of Financing and Investing Activity:	1997	1996
34. Property and Equipment Acquired Under Capital Lease Obligations	$0	$0
35. Property Acquired Under Long-Term Financing Arrangements	$0	$0
36. Other Exchanges of Non-cash Assets or Liabilities	$0	$0

The accompanying notes are an integral part of these statements.

The accompanying notes are an integral part of these statements.

DEFENSE COMMISSARY AGENCY

WORKING CAPITAL FUND

CONSOLIDATED FOOTNOTES TO THE PRINCIPAL STATEMENTS

Footnotes

DEPARTMENT OF DEFENSE
DEFENSE COMMISSARY AGENCY
COMMISSARY OPERATIONS AND RESALE STOCKS
NOTES TO THE PRINCIPAL STATEMENTS
AS OF SEPTEMBER 30, 1997

Note 1. Significant Accounting Policies

A. Basis of Presentation:

These financial statements have been prepared to report the financial position and results of operations of the Department of Defense (DoD), as required by the Chief Financial Officers Act. They have been prepared from the financial records of the Department in accordance with DoD Accounting policies which are summarized in this note. These statements, therefore, are different from the financial reports, also prepared by the DoD pursuant to OMB directives, that are used to monitor and control DoD's use of budgetary resources.

B. Reporting Entity:

DeCA Headquarters maintains overall program and fund control for funds distribution and execution reporting. The headquarters staff issues fund targets to the three CONUS commissary regions and to the OCONUS (European) region.

On October 1, 1996, DeCA was inaugurated by the Department of Defense as a performance based organization (PBO). PBO's are part of an overall Government reinvention program called the National Performance Review, sponsored by the White House and managed by the Vice President, who nominated DeCA as one of the eight Federal Agencies in March 1996, to become a PBO. DeCA's PBO status will allow the Agency to become more efficient and business-like in its management of commissaries worldwide.

On December 11, 1996, the Under Secretary of Defense (Comptroller) canceled the Defense Business Operations Fund and established four funds: the Army Working Capital Fund, the Navy Working Capital Fund, the Air Force Working Capital Fund, and the Defensewide Working Capital Fund. Collectively, the four funds are known as the Defense Working Capital Funds (DWCF). The DWCF embodies the principles of the National Performance Review: cutting unnecessary spending, servicing customers, empowering employees, and helping organizations solve their own problems.

Centralized accounting support for the CONUS regions, Headquarters and the Operations Support Center (OSC) is provided by the Defense Finance and Accounting Service Columbus Center (DFAS-CO), at Columbus, Ohio. The Defense Business Management System (DBMS) is used at DFAS-CO to account for the DWCF Commissary Operations. DBMS provides complete accounting control of funds distribution, commitments, obligations, expenses, disbursements, collections and reimbursements. The system also produces financial reports containing the results and status of operations. Commissary Resale Stocks are accounted for using the Standard Finance System (STANFINS). CONUS region liaison offices interface with DFAS for payroll matters and other accounting requirements.

The Commissary Operations Fund is used for all civilian labor and related personnel costs and operating, equipment and supply costs above the commissary level.

Centralized accounting support for the European Region is provided by the 266 Theater Finance Command, at the Subsistence Finance and Accounting Office (SFAOE) in Germany. STANFINS is used for all DeCA accounting activity in Europe.

Effective October 1994, DFAS-CO assumed full responsibility for the preparation and submission of agency-level reports for DeCA. Both centralized accounting support offices provide accounting reports to the Agency Reporting Division (DFAS-CO-AC), where they are consolidated and submitted to the Departmental Accounting Office at the DFAS-Indianapolis Center.

In CONUS, resource management personnel in region liaison offices input commissary operations and surcharge-funded commitments, obligations and expenses into the DBMS system over dedicated communication lines. Supporting documents are forwarded to DFAS-CO, while copies are also retained at the regions. The regions also perform reviews of unliquidated obligations. DFAS-CO maintains DeCA's CONUS activity records, process and issue billings, provides commercial accounts service, process travel and permanent change of station (PCS) payment, provides collection and disbursement services, and provides civilian payroll services for those DeCA organizations paid in DBMS. They also provide DeCA with activity reports for DeCA funds executed through DFAS-CO.

The European Region obtains support from the SFAOE to include accounting and reporting for assigned funds; commercial accounts for offshore acquisitions; collection/disbursement services; billing; processing TFO/TBO transactions and travel/PCS. Accounting reports from STANFINS are provided monthly to the Region, DFAS-CO and DeCA Headquarters by the SFAOE.

In CONUS, obligations and receipts for subsistence delivery orders are generated simultaneously and forwarded electronically each business day from the commissaries into a computer located at the OSC. The data is loaded in the Standard Automated Voucher Examination System (SAVES), where the accounting transactions are produced. A SAVES transaction file is transmitted to the computer center at Columbus, and interfaced into the Automated System for Army Commissaries (ASAC) and STANFINS. Supporting documents are retained at the commissaries and DFAS-CO East and West Service Centers.

Milstrip Fresh Fruit and Vegetable (FF&V) requisitions are issued for resale subsistence. The requisition data is transmitted electronically from the commissary or Central Distribution Center (CDC) to the OSC computer. Each workday, the OSC computer passes a transaction file to Columbus, where the obligations are interfaced into ASAC and STANFINS.

The OSC was provisionally established December 4, 1994, and became fully operational on October 1, 1995. The OSC provides direct operational support to commissaries, regions, and zone managers. Its functional elements include: contracting, accounting, transportation, marketing, logistics, and information operations. The OSC is organized into multi-functional business units (teams) around major business processes. The OSC performs resource management functions related to CONUS stock fund bill paying, and reconciliation of CONUS stock fund inventory supply records with the financial records. The OSC has an added mission to manage the DeCA worldwide merchandise coupon redemption program which includes oversight of processing from acceptance to redemption; accounting for redemptions and losses; and processing documentation to return the cash to the resale stock fund. The Marketing Business Unit (MBU) formed in 1994, addresses and resolves operational issues spanning Electronic Data Interface (EDI), contracting for brand name resale products, merchandising at national levels, cataloging, electronic pricing, and other support for store level operations. The MBU is part of the OSC.

The DFAS-CO East and West Service Centers generate payment vouchers for resale commercial accounts for DeCA CONUS region commissaries. The voucher and check-producing information is passed electronically from the OSC computer to DFAS-CO, where checks or EFT payments are produced and forwarded to vendors, and the accounting records are updated. DFAS-CO Service Centers retain documents to support vendor payments. DFAS-CO provides check numbers to the Service Center to update the SAVES automated bill registers. The DeCA European region commercial payments are made by the SFAOE using the Computerized Accounts Payable System (CAPS). The voucher and check producing information is generated by the Army Disbursing Office Payment System (DOPS). DeCA plans to implement SAVES in Europe during FY 98.

Due to a reengineering change, DeCA has assumed the acquisition and distribution functions of the Defense Personnel Support Center (DPSC) in support of commissaries, except for fresh fruits and vegetables, and offshore acquisition. Contracts for specific meats, bread and dairy products are now awarded by DeCA. Requisitions for semi-perishable and perishable brand name products overseas are being supported by the DeCA Interim Business System (DIBS) and DeCA Overseas Ordering and Receiving System (DOORS). The perishables distribution center in Europe, which was used to contain DPSC wholesale stock, is now used to contain DeCA retail stock.

Collections affect all three funds provided DeCA to operate the commissaries. Daily commissary sales receipts and surcharge collections (five percent added to sales price at checkout) are deposited into the DWCF Resale Stocks account and the Commissary Surcharge Collections account, respectively. The face values of merchandise coupon redemptions are deposited into Commissary Resale Stocks; reimbursement for coupon handling goes into the DWCF Commissary Operations account.

C. Budget and Budgetary Accounting:

Budget authority is received on the DD Form 1105R, Apportionment and Reapportionment Schedule. For Commissary Operations, budget authority is apportioned on the DD Form 1105R. For Resale Stocks, obligations may be incurred up to the amount of revenues generated by sales to customers. Both funds operate subject to the provisions of 31 USC 1517, relevant sections of 10 USC and DoD 1330.17-R.

D. Basis of Accounting:

Transactions are recorded on an accrual accounting and budgetary basis. Under the accrual method, revenues are recognized when earned, and expenses are recognized when a liability is incurred, without regard to receipt or payment of cash. Budgetary accounting/reporting is performed in compliance with OMB requirements.

E. Revenues and Other Financing Sources:

Resale Stock revenues are generated from sale of inventory items to authorized commissary patrons, whether on a cash, credit/debit cards, or charge sale basis. These inventory items consist of grocery, meat, and produce. Commissary Operations revenues are generated from coupon handling fees and from miscellaneous services provided for authorized customers. Revenues are recognized when earned.

F. Accounting for Intra-governmental Activities:

These statements are prepared net of intra-agency eliminations.

G. Funds with the U.S. Treasury and Cash:

DeCA's fund resources are maintained in Treasury accounts. It's cash receipts and disbursements are processed by the Treasury, and the balance with the Treasury represents the aggregate of all unexpended balances.

H. Foreign Currency: Not Applicable

I. Accounts Receivable:

The accounts receivable is presented in the Consolidated Statement of Financial Position. This account includes government, public, and Vendor Credit Memorandum (VCM) accounts and refunds receivables. Allowances for uncollectible accounts are based upon analysis of receivables aged over 180 days old. During fiscal year 1997, the DeCA wrote off approximately $5,192 in uncollectible receivables.

J. Loans Receivable: Not Applicable

K. Inventories: Inventories, including operating supplies and non-consumable items, are valued at Latest Acquisition Cost as required by DoD accounting policies. Generally, these values are based on prices paid for recently acquired items. Gains and losses that result from valuation changes for inventory items are recognized and reported in the Statement of Operations and included in the calculation of the cost of goods sold.

L. Investments in U. S. Government Securities: Not Applicable

M. Property and Equipment:

DeCA utilizes the Defense Property Accountability System (DPAS) to account for property and equipment. This data is interfaced with DBMS and monthly reconciliations are performed. DPAS does not interface with STANFINS; therefore, journal vouchers are prepared to update the system. The monthly property and equipment reports are produced from DPAS.

N. Prepaid and Deferred Charges: Not Applicable

O. Leases: Not Applicable

P. Contingencies: Not Applicable

Q. Accrued Leave:

Civilian annual leave is accrued as earned and the accrued amounts are reduced as leave is taken. The balance for annual leave is adjusted at the end of the fiscal year to reflect current pay rates for the leave that is earned but not taken. Sick and other types of nonvested leave are expensed as taken. To the extent current or prior year appropriations are not available to fund annual leave earned but not taken, funding will be obtained from future financing sources.

R. Equity: Not Applicable

S. Aircraft/Ship Crashes: Not Applicable

T. Treaties for Use of Foreign Bases: Not Applicable

U. Comparative Data: Not Applicable

V. Undelivered Orders: Not Applicable

Note 2. Fund Balance With Treasury

A. Working Capital Fund (USD(C)) and All Other Funds and Accounts:

	Trust Funds	Revolving Funds	Entity Assets Appropriated Funds	Other Fund Types	Total
Unobligated Balance Available:					
Available	$ 0	$ 0	$ 0	$ 0	$ 0
Restricted	$ 0	$ 0	$ 0	$ 0	$ 0
Reserve for Anticipated Resources	$ 0	$ 0	$ 0	$ 0	$ 0
Obligated	$ 0	$ 0	$ 0	$ 0	$ 0
Unfunded Contract Authority	$ 0	$ 0	$ 0	$ 0	$ 0
Unused Borrowing Authority	$ 0	$ 0	$ 0	$ 0	$ 0
Treasury Balance	$ 0	$ 0	$ 0	$ 0	$ 0

B. Working Capital Fund Activities Below (USD(C)) Level:

	Appropriated Funds	Entity Assets Funds Collected	Entity Assets Funds Disbursed
Beginning Balance	$ 0	$ 0	$ 0
Transfer of Cash to Others	$ 0	$ 0	$ 0
Transfer of Cash from Others	$ 0	$ 0	$ 0
Funds Collected	$ 0	$ 5,080,346	$ 0
Funds Disbursed	$ 0	$ 0	$ (6,213,094)
1997 Treasury Warrant	$ 935,935	$ 0	$ 0
Ending Balance	$ 935,935	$ 5,080,346	$ (6,213,094)

C. All Funds and Accounts.

	NonEntity Assets Funds Collected	NonEntity Assets Funds Disbursed
Beginning Balance	$ 0	$ 0
Funds Collected	$ 0	$ 0
Funds Disbursed	$ 0	$ 0
Ending Balance	$ 0	$ 0

D. Other Information: For 5J00, the Fund Balance with Treasury amount includes adjustments for undistributed collections of $5,088 and undistributed disbursements of $12,724. Also included in undistributed disbursements is a DWCF Corporate Accounts Transfer of $30,000. The original Treasury Warrant issued for 5J00 is $917,300. This amount decreased by $862, directed by a Program Budget Decision, to use for anti-terrorism. Also included in the amount is $19,497 for Reprogramming Action FY 97-PA. Collections include $7,438 which was not reported to Treasury and therefore is not included in Treasury amounts. This amount is a cost recovery fee from tobacco sales from DeCA Surcharge to DeCA Operations.

Fund Balance With Treasury (5K00) reported above consists of collections and disbursements that have been reconciled to financial reports at Treasury. Funds disbursed per activity records show general ledger account balances of $(5,195,491). The difference of $16,047 consists of undistributed disbursements recorded in the automated accounting system, but have not yet been processed by Treasury. Funds collected per activity records show general ledger account balances of $5,130,582. The difference of $(99,959) consists of undistributed collections of $(805) and PY undeposited collections of $(99,154).

Last year, collections reported on the financial statements were overstated by $99,154 over amounts reported in the automated accounting system, and receivables were understated by the same amount. This is attributed to the method of reporting undeposited collections (cash sales) in prior year. Although cash sales are recorded as receivables in the accounting system, FY 1996 year end financial statements reduced receivables by $99,154 and reported these funds as collections. Based on a joint conference between DFAS and DeCA in April 1997, a decision was made to begin reporting cash sales as receivables on prepared financial statements.

Since collections were overstated by $99,154 on prior year end financial statements, collections reported on current year reports must be reduced by the same amount. The net effect on reported net cash outlays and Fund Balance with Treasury between both reporting years will be zero. Although this adjustment will reconcile the reported fund balance, it greatly distorts current year net outlays for DeCA.

Note 3. Cash, Foreign Currency and Other Monetary Assets Not Applicable

Note 4. Investments Not Applicable

Note 5. Accounts Receivable

	(1) Allowance Amount Due	(2) Allowance For Estimated Uncollectibles	(3) Method Used	(4) Amount Due
A. Entity Receivables:				
Intragovernmental	$ 7,230		See below	$ 7,230
Governmental	$ 151,482	(2,731)		$ 148,751
B. Non-Entity Receivables:				
Intragovernmental	$ 0	$ 0		$ 0
Governmental	$ 0	$ 0		$ 0

C. Other Information: For 5J00, Allowance was based on 2% of the dollar amount of public receivables over 180 days delinquent. The amount of Intragovernmental receivables includes CY and PY undistributed collections in the amount of $3,512.

For 5K00, the gross receivables of $154,067 reported includes undistributed collections of $805. This adjustment amount to receivables represents the difference of reported collections between the automated accounting system and Treasury records. The gross receivables reported above includes cash sales receivables of $101,197.

The method used for uncollectible accounts is derived by taking 10 percent of public receivables that are aged over 180 days delinquent. During FY 97 the allowance account for uncollectible receivables was adjusted accordingly at the time of the collection or write-off. In FY 97, DeCA wrote off approximately $5,192 in uncollectible receivables.

Aggressive efforts taken by DeCA, DFAS-CO and SFAOE have reduced the outstanding resale charge sale receivables. The implementation of credit card procedures for accepting credit cards from the appropriated fund customers have contributed to the government receivables being reduced from $5.7 million at the end of September 1996, to $3.3 million at the end of September 1997. At this time, the use of credit cards by appropriated fund customers has been limited to CONUS, pending implementation of POS-M in the overseas areas. Full implementation of POS-M will be completed in FY 99. Even though the use of credit cards by non-appropriated fund customers reduced receivables in the area, the overall increase during FY 97 was attributed to the transfer of tobacco products to AAFES and NEXCOM. DeCA sold approximately $40.4 million of existing inventory to the exchanges during FY 97.

See Note 29, Intrafund Eliminations

Note 6. Other Assets Federal (Intragovernmental) and Non Federal (Governmental) Assets Not Applicable

Note 7. Loans and Loan Guarantees, Non Federal Borrowers Not Applicable

Note 8. Inventory, Net

	(1) Inventory Amount	(2) Allowance For Losses	(3) Inventory, Net	(4) Valuation Method
A. Inventory Categories:				
(1) Held for Current Sale	$325,214	2,821	328,035	a
(2) Held in Reserve for Future Sale				
(3) War Reserve Materiel				
(4) Excess, Obsolete, and Unserviceable				
(5) Held for Repair				
Total	$325,214	2,821	328,035	

B. Restrictions on Inventory Use, Sale, or Disposition:

C. Other Information: Inventory Held for Current Sale includes inventory goods ready for sale and inventory-in-transit. Inventory allowance reported on the financial statements values inventory at the latest acquisition cost (LAC) based on sales revenue. The allowance for gains/losses (GLA 1529) was adjusted based on the computation of Cost of Goods Sold.

Note 9. Work in Progress Not Applicable

Note 10. Operating Materials and Supplies (OM&S), Net Not Applicable

Note 11. Stockpile Materials Net Not Applicable

Note 12. Seized Property Not Applicable

Note 13. Forfeited Property, Net Not Applicable

Note 14. Goods Held Under Price Support and Stabilization Programs, Net — Not Applicable

Note 15. Property, Plant and Equipment, Net

	(1) Depreciation Method*	(2) Service Life*	(3) Acquisition Value	(4) Accumulated Depreciation	(5) Net Book Value
Classes of Fixed Assets					
A. Land			$ 0	$ 0	$ 0
B. Structures, Facilities, & Leasehold Improvements			$ 103	$ 0	$ 103
C. Military Equipment			$ 0	$ 0	$ 0
D. ADP Software			$ 0	$ 0	$ 0
E. Equipment	SL		$ 1,142	$1,037	$ 105
F. Assets Under Capital Lease			$ 0	$ 0	$ 0
G. Other			$ 0	$ 0	$ 0
H. Natural Resources			$ 0	$ 0	$ 0
I. Construction in Progress			$ 325	$ 0	$ 325
Total			$ 1,570	$ 1,037	$ 533

*Keys:

Depreciation Methods	Range of Service Life
SL = Straight Line	1 - 5 = 1 to 5 years
DD = Double-Declining Balance	6 - 10 = 6 to 10 years
SY = Sum of the Years' Digits	11 - 20 = 11 to 20 years
IN = Interest (sinking fund)	>20 = Over 20 years
PR = Production (activity or use method)	
OT = Other (describe)	

Other Information: As of the end of Fiscal Year 1997, completed commissaries have been transferred to the host installation. A decision is pending from the DoD Policy, Under Secretary of Defense (Comptroller) on whether the completed commissaries should remain on the property book of the Defense Commissary Agency or be transferred to the installation. The pending decision should also determine if the property should be carried on the property account of the Defense Working Capital Fund or the Titleholder, Surcharge Collections account. Construction of commissaries is funded by Surcharge Collections. The value of commissaries completed since the inception of DeCA is $363,015.

Note 16. Debt — Not Applicable

Note 17. Other Liabilities

A. Other Liabilities Covered by Budgetary Resources:

B. Other Information:

C. Other Liabilities Not Covered by Budgetary Resources:

	Non-Current Liability	Current Liability	Total
1. Intragovernmental			
2. Governmental			
(a) Annual Leave	$30,365		$30,365
(b)	0		0
Total	$30,365		$30,365

Note 18. Leases Not Applicable

Note 19. Pensions and Other Actuarial Liabilities

Major Program Activities	(1) Actuarial Present Value of Projected Plan Benefits	(2) Assumed Interest Rate	(3) Assets Available to Pay Benefits	(4) Unfunded Actuarial Liability
A. Pension and Health Plans	$		$	$
B. Insurance/Annuity Programs	$		$	$
C. Other-Workers Compensation	$		$	$ 64,945
D. Total Line A + B + C	$		$	$ 64,945

E. Other Information:

Future workers' compensation figures are provided by the Department of Labor. The liability for future workers' compensation (FWC) benefits includes the expected liability for death, disability, medical, and miscellaneous costs for approved compensation cases. The liability is determined using a method that utilizes historical benefit payment patterns related to a specific incurred period to predict the ultimate payments related to that period. Consistent with past practice, these projected annual benefit payments have been discounted to present value using the Office of Management and Budget's, June 10, 1997 economic assumptions for 10-year Treasury notes and bonds. Interest rate assumptions utilized for discounting were as follows:

1997

6.24 % in year 1
5.82 % in year 2
5.60 % in year 3
5.45 % in year 4
5.40 % in year 5 and thereafter

Note 20. Net Position

	Revolving Funds	Trust Funds	Appropriated Funds	Total
A. Unexpended Appropriations:				
(1) Unobligated				
a. Available	$ 0	$ 0	$ 0	$ 0
b. Unavailable	$ 0	$ 0	$ 66,666	$ 66,666
(2) Undelivered Orders	$ 0	$ 0	$ 0	$ 0
B. Invested Capital	$ 5,168,537	$ 0	$ 0	$ 5,168,537
C. Cumulative Results of Operations	$(5,463,674)	$ 0	$ 0	$(5,463,674)
D. Other	$ 0	$ 0	$ 0	$ 0
E. Future Funding Requirements	$ (95,310)	$ 0	$ 0	$ (95,310)
F. Total	$ (390,447)	$ 0	$ 66,666	$ (323,781)

G. Other Information: For 5J00, the amount of Unavailable Appropriated Funds represents the amount of the PY Undelivered Orders(56,442) + CY Treasury Warrant (916,438) less Appropriated Capital Used (906,214). Appropriated Capital Used is the amount of current year disbursements, less revenue, less CY reprogramming action (19,497), and + or - change in liabilities from prior year to current year.

For 5K00, Invested Capital includes the initial assets capitalized in October 1991, the inventories capitalized in October 1995 due to assume the acquisition and distribution of the DLA cold storage functions, the inventories decapitalized in October 1995 due to transfer of the Troop Issue functions to the Air Force, and the cumulative funds transferred to Treasury.

Note 21. Taxes Not Applicable

Note 22. Other Revenues and Financing Sources

	1997	1996
A. Other Revenues and Financing Sources:		
(1) Other Miscellaneous Gains	$ 322	$ 1,583
(2) CSRS/FERS Retirement, Federal Employees Health Benefits, Federal Employee Group Life Insurance	$ 58,615	$ 0
Total	$ 58,937	$ 1,583

B. Other Information: The miscellaneous gain account on the general ledger is used to record the write-off of uncollectible receivables (Bad Checks, Charge Sales), the cash sales adjustments, and the miscellaneous checks received from claims filed as a result of Report of Surveys, Transportation Discrepancy Reports, and the Report of Discrepancy (RODs). DFAS-CO prepares a JV monthly to move the amount of the write offs of charge sales and bad checks out of the Other Miscellaneous Gains account to the Allowance for Loss on Receivables account. Depending on the net volume between write-offs and collections during the fiscal year, this account may have either a debit (loss) or credit (gain) balance on the general ledger trial balance.

Imputed Pension and Other Retirement Benefits (ORB):

CSRS/FERS Retirement	$41,193
Health	$17,370
Life Insurance	$ 52

The $58,615 represents the imputed financing for pensions and other retirement benefits. The Office of Personnel Management (OPM) is the administrative entity for pensions and other retirement benefits (ORB). OPM accounts for and reports the pension liability in the financial statements while the employer discloses the imputed financing. OPM actuaries provide the normal cost rates which are used to calculate the imputed financing.

Note 23. Program or Operating Expenses

A. Operating Expenses by Object Classification:

	1997	1996
(1) Personal Services and Benefits	$ 574,987	$ 575,062
(2) Travel and Transportations	$ 160,707	$ 159,604
(3) Rental, Communication and Utilities	$ 1,067	$ 1,105
(4) Printing and Reproduction	$ 185	$ 181
(5) Contractual Services	$ 230,347	$ 242,024
(6) Supplies and Materials	$ 753	$ 1,293
(7) Equipment-Not Capitalized	$ 322	$ 709
(8) Grants, Subsidies and Contributions	$ 1,194	$ 1,214
(9) Other Expenses (Cost of Services)	$ 833	$ 328
(10) Total Expenses by Object Class	$ 970,395	$ 981,520

B. Intra Eliminations	$ (251)
C. Total	$ 970,144

D. Other Information: See Note 29, Intrafund Eliminations

Note 24. Cost of Goods Sold

A. Cost of Services Sold:

(1) Beginning Work-in-Process	$ 0
(2) Plus: Operating Expenses	0
(3) Minus: Ending Work-in-Process	0
(4) Minus: Completed Work for Activity Retention	0
Cost of Services Sold	$ 0

B. Cost of Goods Sold from Inventory (using Latest Acquisition Cost):

(1) Beginning Inventory - L.A.C.	$ 342,812
(2) Less: Beginning Allowance for Unrealized Holding Gains (Losses)	4,207
(3) Plus: Purchases at Cost	5,152,227
(4) Plus: Customer Returns - Credit Given	0
(5) Plus: DLR Exchange Credits	0
(6) Less: Inventory Losses Realized	(36)
(7) Less: Ending Inventory - L.A.C.	(325,214)
(8) Plus: Ending Allowance for Unrealized Holding Gains (Losses)	(2,821)
(9) Less: Equity Transfers of Inventory to Others	(192)
(10) Plus: Equity Transfers of Inventory from Others	123
(11) Equals: Cost of Goods Sold from Inventory	$5,171,106

C. Intra Eliminations	$ (2,049)
D. Total	$5,169,057

E. Other Information: The breakout of Cost of Goods Sold between governmental (public) and Intragovernmental sources reported on Lines 10A and 10B on the Statement of Operations is based upon sales revenue that is generated from within and outside the government. Both beginning and ending allowance accounts are adjusted to reflect inventory gains and losses at the latest acquisition cost (LAC) versus standard price as reported in the automated accounting system.

Under current DeCA policy, discounts earned in the Resale Stocks fund are transferred each month to the Surcharge Collection fund as revenue. This causes COGS for Resale Stocks to be higher than if the discounts earned were retained in the Resale account. Initially, the dollar value of discounts earned is recorded in the Resale Stocks fund as a reduction to COGS/expenses. At month end, these funds are reversed out of the Resale Stocks fund, and electronically transferred over to the Surcharge Collection fund as an increase to revenue. The net effect on accumulative operating results (AOR) between both funds is zero. This accounting practice has overstated expenses this fiscal year for Resale Stocks by $17.8 million on prepared financial statements. AOR reported through FY 1996 for Resale Stocks has been overstated by $65 million.

See Note 29, Intrafund Eliminations

Note 25. Other Expenses

	1997	1996
A. Other Expenses:		
(1) Loss on Disp of Cap Assets	$ 0	$ 11
(2) Inventory Losses	$ 36	$ 311
(3) CSRS/FERS, FEHB, FEGLI	$ 58,615	$ 0
Total	$ 58,651	$ 322

B. Other Information:

Imputed Pension and Other Retirement Benefits (ORB):

CSRS/FERS Retirement	41,193
Health	17,370
Life Insurance	52

The $58,615 represents the imputed expense for pensions and other retirement benefits. The Office of Personnel Management (OPM) is the administrative entity for pensions and other retirement benefits (ORB). OPM accounts for and reports the pension liability in their financial statements while the employer discloses the imputed expenses. OPM actuaries provide the normal cost rates which are used to calculate the imputed expenses.

Note 26. Extraordinary Items Not Applicable

Note 27. Prior Period Adjustments

A. Prior Period Adjustments:

(1) Prior Year Expenses $ (250,833)

Note 28. Non-Operating Changes - (Transfers and Donations)

	1997		1996	
A. Increases:				
(1) Transfers-In:				
(a) Real Property Maintenance	$	544	$	194
(b) Capitalized Assets	$	0	$	389
(c) Net Capital Equipment	$	87	$	327
(d) Advance	$	1,194	$	0
(e) Transfers-In	$	518	$	0
(2) Donations Received	$	0	$	0
(3) Other Increases	$	0	$	0
(4) Total Increases	$	2,343	$	910
B. Decreases:				
(1) Transfers-Out:				
(a) Funds with Treasury PY	$	(202,508)	$	(518,907)
(b) CY - PY Approp Avail (66,666-56,442)	$	(10,224)	$	(56,442)
(c) DPAS Transfer	$	0	$	(136)
(d) Building	$	0	$	(119)
(e) PY DLA Transfer, Adjusted CY	$	(251,600)	$	0
(f) Reprogramming Action FY 97-PA	$	(19,497)	$	0
(g) Inventory Trans Out to Govt. Agencies	$	192	$	39,439
(h) Funds Transferred Out to Treas	$	(50,100)	$	(17,292)
(2) Donations	$	0	$	0
(3) Other Decreases(Unfunded Work Comp Liab)	$	64,945	$	0
(4) Total Decreases	$	(468,792)	$	(553,457)
C. Net Non-Operating Changes (Transfers):	$	466,449	$	552,547

Note 29. Intrafund Eliminations:

Schedule B: ELIMINATING ENTRIES

Selling Activity:	Column A Accounts Receivable	Column B Revenue	Column C Unearned Revenue	Column D Collections
DeCA	2	2,300	0	2,123
TOTAL	2	2,300	0	2,123

Customer Activity:	Column A Accounts Payable	Column B Expenses	Column C Advances	Column D Disbursements
(SRC/CD)				
A00 Trust Fund Accts	2	7	0	81
100 Intra-Approp.Reimb	0	2,042	0	2,042
400 DoD Sources (Other Defense Accts)	0	251	0	0
414 DLA (Oth than 418) Btwn DLA	0	251	0	0
Undistributed	N/A	N/A	N/A	N/A
TOTAL	2	2,300	0	2,123

Schedule C: ELIMINATING ENTRIES

Selling Activity:	Column A Accounts Receivable	Column B Revenue	Column C Unearned Revenue	Column D Collections
DeCA	6,532	31,303	0	38,563
TOTAL	6,532	31,303	0	38,563

Customer Activity:	Column A Accounts Payable	Column B Expenses	Column C Advances	Column D Disbursements
(SRC/CD)				
100 Navy, Marine Corp	60	1,481	0	1,642
200 Army Reimb	541	6,286	0	6,557
300 Air Force Reimb	451	13,898	0	16,199
400 Navy Reimb	1,789	8,421	0	8,247
700 Dept of Defense	86	825	0	813
Undistributed	3,605	392	N/A	5,105
TOTAL	6,532	31,303	0	38,563

Schedule D: ELIMINATING ENTRIES

Selling Activity:	Column A Accounts Receivable	Column B Revenue	Column C Unearned Revenue	Column D Collections
DeCA	698	3,603	0	3,461
TOTAL	698	3,603	0	3,461

Customer Activity:	Column A Accounts Payable	Column B Expenses	Column C Advances	Column D Disbursements
(SRC/CD)				
800 Other Govt Depart	698	3,603	0	3,461
TOTAL	698	3,603	0	3,461

For 5K00, revenues exceed earnings due to write-offs of uncollectible accounts. The proforma transaction code currently used to write-off receivables reduces earnings on the budgetary general ledger trial balance, but does not effect revenues recorded on the proprietary accounts.

Note 31. Other Disclosures

A. Unmatched Disbursements, Negative Unliquidated Obligations, and Aged In-Transit Disbursements.

	September 1996	September 1997	Dollar Change	Percent Change
Unmatched Disbursements	3,515	4,343	828	24%
Negative Unliquidated Obligations	739	2,866	2,127	288%
TOTALS	4,254	7,209	2,955	69%

B. Other Information: For 5K00, Quarterly joint reviews were conducted during the year to include the unliquidated obligations reviews, negative undelivered orders, stand alone disbursements, and receipts greater than disbursements.

C. Unexpended Appropriations/Appropriated Capital Used

For 5J00, these lines reflect a change in policy regarding the reporting of the Treasury Warrant. Prior to 1996, the warrant was not included in departmental reporting financial statements. Prior year appropriation amounts have been adjusted as Agency Component Adjustments. In 1997, the amount of Unexpended Appropriation (66,666) is the amount of the PY Undelivered Orders (56,442) + CY Treasury Warrant (916,438) less Appropriated Capital Used (906,214). Appropriated Capital Used is the amount of current year disbursements (1,033,650), less revenue (45,199), less CY reprogramming action (19,497), and - (62,740) change in liabilities from prior year to current year.

Appendix D. Audit Opinion

This appendix (a total of 3 pages) consists of the audit opinion.

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

February 27, 1998

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER) AND CHIEF FINANCIAL OFFICER
DIRECTOR, DEFENSE COMMISSARY AGENCY
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE

SUBJECT: Disclaimer of Opinion on the Defense Commissary Agency Financial Statements for FY 1997 (Project No. 7FH-2042)

The Chief Financial Officers (CFO) Act of 1990, as amended by the Federal Financial Management Act of 1994, requires financial statement audits by the Inspectors General and prescribes the responsibilities of management and auditors for the financial statements, internal controls, and compliance with laws and regulations. Directors of the DoD agencies are responsible for establishing and maintaining an internal control structure and for complying with laws and regulations applicable to DoD. Our responsibility is to render an opinion on the financial statements based on our work, and to determine whether internal controls were adequate and whether the Defense Commissary Agency (DeCA) complied with laws and regulations.

Before FY 1992, the DoD operated a significant number of commercial and industrial facilities under a revolving fund concept. In FY 1992, the revolving funds were consolidated to form the Defense Business Operations Fund (DBOF). The Inspector General, DoD, was responsible for auditing and rendering an opinion on the DBOF consolidated financial statements. In December 1996, the Under Secretary of Defense (Comptroller) restructured the DBOF into separate working capital funds.

Disclaimer of Opinion. We were unable to render an opinion on the DeCA Consolidated Financial Statements for FYs 1997 and 1996. The DeCA Consolidated Financial Statements consisted of statements for DeCA Operations and DeCA Resale Stock Fund. We did not audit the financial statements for DeCA Operations. In addition, we did not receive the financial statements in a timely manner; therefore, we could not determine the accuracy and completeness of the data reported. Also, we were unable to observe a physical inventory (77 percent of the Commissary Resale Stock Fund total assets) at any commissary. Therefore, the scope of our work was limited. For the work we did perform on the FY 1997 DeCA Resale Stock Fund Financial Statements, we reviewed selected internal controls and aspects of compliance with laws and regulations. Although progress has been made, significant deficiencies in the accounting systems and the lack of a sound internal control structure prevented the preparation of accurate financial statements. Without a sound internal control structure, management cannot rely on the FYs 1997 and 1996 DeCA Resale Stock Fund Financial Statements for making decisions or assessing performance.

Accounting Principles. The DeCA financial statements for FYs 1997 and 1996 were to be prepared in accordance with Office of Management and Budget (OMB) Bulletin No. 94- 01, "Form and Content of Agency Financial Statements," November 16, 1993, as supplemented by OMB Bulletin No. 97-01, "Form and Content of Agency Financial Statements," October 16, 1996. These Bulletins incorporate the

Statements of Federal Financial Accounting Concepts and Standards recommended by the Federal Accounting Standards Advisory Board, which are approved by the Secretary of the Treasury; the Director, OMB; and the Comptroller General of the United States. Footnote 1 of the FY 1997 DeCA Resale Stock Fund Financial Statements discusses the significant accounting policies that DeCA followed in preparing the financial statements.

Internal Controls. Internal controls for the FYs 1997 and 1996 DeCA Resale Stock Fund Financial Statements were not adequate. Specifically, internal controls for the accounting systems did not provide reasonable assurance that financial information was reliable. The U.S. Government Standard General Ledger had not been implemented for the Standard Finance System (STANFINS), and STANFINS was noncompliant in 5 of the 13 key accounting requirements, including property and inventory accountability and cost accounting. The Standard Finance System Redesigned (SRD-1) did not have edit checks to ensure the timely processing of disbursement data, which would affect the Fund Balance With Treasury, Accounts Receivable, and Accounts Payable. In addition, the expense accounts of the DeCA Resale Stock Fund were overstated by $15.6 million on the FY 1996 Statement of Operations because expenses were not properly recorded.

Compliance With Laws and Regulations. We assessed compliance with laws and regulations related to the financial statements. Noncompliance with laws and regulations is a reportable condition if the noncompliance could result in material misstatements in the financial statements, or if the sensitivity of the matter would cause anyone to perceive the noncompliance as significant.

Noncompliance with laws and regulations continued to exist at the Defense Finance and Accounting Service (DFAS), the preparer of the DeCA financial statements. Accounting systems and internal controls did not completely or accurately disclose the financial condition of the agency, as required by title 31, United States Code. Under the Federal Financial Management Improvement Act of 1996 and OMB Bulletin No. 93-06, Addendum 1, "Audit Requirements for Federal Financial Statements," January 16, 1998, our work disclosed that financial management systems did not comply with Federal financial management system requirements; applicable Federal accounting standards; and the United States Government Standard General Ledger at the transaction level. Also, DFAS did not always comply with DoD 7000.14-R, the "DoD Financial Management Regulation," in the recording of Accounts Payable and Fund Balance With Treasury. DoD 7000.14-R requires Accounts Payable to exclude purchase discounts. Currently, Accounts Payable (86 percent of the total liabilities for Commissary Resale Stock Fund) is being reported at the full amount. Consequently, Accounts Payable was misstated in the FY 1997 DeCA Resale Stock Fund Financial Statements. Also, DFAS is not promptly reconciling differences shown on the Statement of Differences issued by the Department of the Treasury. Consequently, the Fund Balance with Treasury (35 percent of the Commissary Resale Stock Fund total assets) will be misstated.

The FY 1997 DeCA Resale Stock Fund Financial Statements overstated expenses by $17.8 million. This occurred because DeCA policy required purchase discounts earned to be transferred to the Surcharge Collection Fund as revenue. Because purchase discounts are not retained in the Resale Stock Fund Financial Statements, Cost of Goods Sold for Resale Stock is overstated by the amount of the purchase discounts. Currently, DFAS and the Under Secretary of Defense (Comptroller) are determining how purchase discounts should be reported. Also, erroneous collection information was reported to the Department of the Treasury, and $30 million in Undistributed Disbursements was transferred from the Defense Working Capital Fund Corporate Account to the Fund Balance With Treasury Account. As a result, the Fund Balance With Treasury Account could not be validated.

Additional Reports. This memorandum briefly summarizes the major deficiencies affecting DeCA. We will issue subsequent reports with more details on internal controls and compliance with laws and regulations.

David K. Steensma

David K. Steensma
Deputy Assistant Inspector General
for Auditing

Appendix E. Management and Legal Representation Letters

This appendix (a total of 4 pages) consists of the management and legal representation letters for DeCA Financial Statements for FY 1997.

DEFENSE COMMISSARY AGENCY
HEADQUARTERS
1300 E AVENUE
FORT LEE, VIRGINIA 23801-1800

REPLY TO
ATTENTION OF

RMA

February 27, 1998

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING

SUBJECT: Management Assurance Concerning FY 1997 Defense Commissary Agency Working Capital Fund Financial Statements

This is in regard to your audit of the FY 1997 Defense Commissary Agency Working Capital Fund Financial Statements (Project No. 7FH-2042). For the purpose of expressing an opinion as to whether the financial statements are presented fairly in accordance with the other comprehensive basis of accounting described in Office of Management and Budget (OMB) Bulletin No. 94091, "Form and Content of Agency Financial Statements," November 16, 1993, and applicable portions of OMB Bulletin No. 97-01, "Form and Content of Agency Financial Statements," October 16, 1996, we confirm, to the best of our knowledge and belief, the following representations made to you during your audit.

1) We are responsible for the fair presentation of the FY 1997 Defense Commissary Agency Working Capital Fund Financial Statements in accordance with OMB Bulletin No. 94-01 and applicable portions of OMB Bulletin No. 97-01.

2) We have made available to you all financial records and related data.

3) We can provide reasonable assurance that the accounting and non-accounting systems used to produce the financial statements are reliable.

4) We have no plans or intentions, other than those previously disclosed to you, that may materially affect the carrying value or classification of assets and liabilities.

5) There have been no irregularities involving management or employees who have significant roles in the internal control structure.

6) No other employees have been involved in irregularities that could materially affect the financial statements.

7) We have received no communications from regulatory agencies or auditors concerning noncompliance with, or deficiencies in, financial reporting practices that could have a material effect on the financial statements.

8) There are no violations or possible violations of laws or regulations whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency.

9) There are no other material liabilities or gain or loss contingencies that are required to be accrued or disclosed by Statement of Federal Financial Accounting Standard (SFFAS) No. 5 "Accounting for Contingencies," December 1995.

10) There are no unasserted claims or assessments that our legal representatives have advised us must be disclosed in accordance with SFFAS No. 5.

11) There are no material transactions that have not been properly recorded in the accounting records and reflected in the financial statements.

12) The Department of Defense has satisfactory title to all assets, and there are no liens or encumbrances on such assets, nor has any asset been pledged.

13) No events have occurred after the balance sheet date that should require adjustments to, or disclosure in, the financial statements.

14) We cannot attest to the accuracy of the various account balances provided by the Defense Finance and Accounting Service and used by DFAS to prepare the financial statements. We do not accept the Collection and Disbursement figures in the Financial Statements as being accurate. During FY 1997, Collection information was reported to the Department of the Treasury incorrectly as reverse Disbursements. The Defense Finance and Accounting Service, Columbus Center submitted monthly adjustments to Treasury via the DELMARS RCS 302 report; however, we cannot determine that all adjustments have been posted by Treasury. Additionally, Undistributed Disbursements contain a transfer from the Defense Working Capital Fund Corporate Account of $30 million. The $30 million was allocated to DeCA based on an estimate of prior period undistributed disbursements and collections. We cannot validate that each individual transaction comprising the $30 million belongs to DeCA. The transfer increased DeCA's Disbursement account balance and decreased the Accounts Payable account balance.

15) All adjustments , with the exception as noted in number 14, made to account balances by our activity or the Defense Finance and Accounting Service are fully documented and were made in accordance with applicable accounting standards.

Gary G Lutz

GARY G. LUTZ
Chief Financial Officer

DEFENSE COMMISSARY AGENCY
HEADQUARTERS
1300 E AVENUE
FORT LEE, VIRGINIA 23801-1800

GC

February 27, 1998

MEMORANDUM FOR GENERAL COUNSEL, DEPARTMENT OF DEFENSE

FROM: GENERAL COUNSEL, DEFENSE COMMISSARY AGENCY

SUBJECT: Inspector General, Department of Defense, Audit of FY 1997 Defense Commissary Agency Working Capital Fund Financial Statements (Project No. 7FH-2042)

The Defense Commissary Agency has no Pending or Threatened Litigation, Claims and Assessments that meet the definition of material to the Defense Working Capital Fund. Additionally, DeCA has no Unasserted Claims and Assessments that have a reasonable possibility of unfavorable outcome.

WILLIAM E. SHERMAN
General Counsel

Appendix F. Laws and Regulations Reviewed

Title 31, U.S. Code, subtitle III, "Financial Management," section 3512, "Executive Agency Accounting and Other Financial Management Reports and Plans"

Public Law 101-576, "Chief Financial Officers Act of 1990," November 15, 1990

Public Law 104-208, "Federal Financial Management Improvement Act of 1996," September 30, 1996

OMB Bulletin No. 98-04, "Addendum to OMB Bulletin No. 93-06," January 16, 1998

OMB Bulletin No. 97-01, "Form and Content of Agency Financial Statements," October 16, 1996

OMB Bulletin No. 94-01, "Form and Content of Agency Financial Statements," November 16, 1993

OMB Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993

OMB Circular No. A-127, "Financial Management Systems," July 23, 1993

OMB Circular No. A-123, "Management Accountability and Control," June 21, 1995

Treasury Financial Manual 2-3100, "Instructions for Disbursing Officers' Reports," April 1, 1997

DoD 7000.14-R, "DoD Financial Management Regulation," volume 4, January 1995: chapter 2, "Accounting for Cash and Fund Balances with Treasury;" chapter 9, "Accounts Payable;" chapter 18, "Revenues"

DoD 7000.14-R, "DoD Financial Management Regulation," volume 5, May 1996: chapter 5, "Deposit and Transfer of Public Funds;"

DoD 7000.14-R, "DoD Financial Management Regulation," volume 11B, December 1994: chapter 59, "Liabilities"

DoD Directive 5010.38, "Management Control Program," August 26, 1996

DeCA Directive 70-2, "Management Control Program," August 30, 1996

Appendix F. Laws and Regulations Reviewed

DeCA Directive 70-3, "Management Control Plan," August 30, 1996

DeCA Directive 70-6, "Financial Procedures for Commissary Management Support Center," July 23, 1993

DeCA Directive 70-7, "Financial Management for Headquarters and Regions," August 31, 1994: chapter 22, "Accountability Variance Statement"

DeCA Directive 70-10, "Procedures for Processing and Paying Commercial Accounts Using SAVES," August 31, 1994

DeCA Directive 70-16, "Financial Management for Service Centers," August 31, 1994

DeCA Directive 40-21(C2), "Subsistence Accountability Inventory Procedure," July 15, 1995

Appendix G. 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)
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

Defense Organizations

Director, Defense Commissary Agency
Director, Defense Contract Audit Agency
Director, Defense Finance and Accounting Service
  Director, Defense Finance and Accounting Service Columbus Center
Director, Defense Logistics 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

Part III - Management Comments

Defense Commissary Agency Comments

DEFENSE COMMISSARY AGENCY
HEADQUARTERS
1300 E AVENUE
FORT LEE, VIRGINIA 23801-1800

REPLY TO
ATTENTION OF

IR

MAY 28 1998

MEMORANDUM FOR INSPECTOR GENERAL, FINANCE AND ACCOUNTING DIRECTORATE, 400 ARMY NAVY DRIVE, ARLINGTON, VA 22202-2884

SUBJECT: Audit Report on Internal Controls and Compliance With Laws and Regulations for the Defense Commissary Agency Financial Statements for FY 1997 (Project No. 7FH-2042.01)

Reference: DoDIG Memorandum, April 29, 1998, SAB

Attached is the DeCA reply to recommendation 2 provided in subject report. If you have any questions, please contact Mr. Ben Mikell at (804) 734-8103.

Donna J. Willis

DONNA J. WILLIS
Executive Assistant for Support

Attachment:
As Stated

DEFENSE COMMISSARY AGENCY REPLY

SUBJECT: Audit Report on Internal Controls and Compliance With Laws and Regulations for the Defense Commissary Agency Financial Statements for FY 1997 (Project No. 7FH-2042.01)

Recommendation 2. We recommend that the Director, Defense Commissary Agency, clarify and standardize procedures related to forwarding deposits and debit information to the Defense Finance and Accounting Service Columbus Center in order to expedite the reconciliation of deposits between commissaries and the Defense Finance and Accounting Service Columbus Center.

DeCA Reply. DeCA concurs with this recommendation. Procedures related to forwarding deposit and debit information will be clarified in DeCA Directive 70-6. The target date for publication of the revised directive is September 30, 1998.

Audit Team Members

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

F. Jay Lane
Salvatore D. Guli
David F. Vincent
Barbara A. Sauls
Jenniffer F. Wilson
Stephanie F. Mandel
Stacey L. Volis
Susanne B. Allen
Angela D. Clayton