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COMPILATION OF FY 1997 AIR FORCE GENERAL FUNDS  
CONSOLIDATED FINANCIAL STATEMENTS AT THE DEFENSE  
FINANCE AND ACCOUNTING SERVICE DENVER CENTER

Report No. 99-004

October 5, 1998

Office of the Inspector General  
Department of Defense

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### **Acronyms**

AFAA	Air Force Audit Agency
CFO	Chief Financial Officers
COARS	Command On-Line Accounting and Reporting System
DFAS	Defense Finance and Accounting Service
DJAS	Defense Joint Accounting System
EIMSURS	Equipment Inventory, Multiple Status and Utilization Reporting System
FMFIA	Federal Managers' Financial Integrity Act
GAO	General Accounting Office
GFGL	General Funds General Ledger
IG	Inspector General
MAFR	Merged Accountability and Fund Reporting
OMB	Office of Management and Budget
PP&E	Property, Plant, and Equipment
SOF	Status of Funds



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

October 5, 1998

MEMORANDUM FOR DIRECTOR, DEFENSE FINANCE AND ACCOUNTING  
SERVICE

SUBJECT: Audit Report on Compilation of FY 1997 Air Force General Funds  
Consolidated Financial Statements at the Defense Finance and Accounting  
Service Denver Center (Report No. 99-004)

We are providing this report for review and comments. This audit was performed in response to the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The Defense Finance and Accounting Service did not comment on a draft of this report. Accordingly, we request the Defense Finance and Accounting Service provide comments on the final report by October 30, 1998.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Brian Flynn at (703) 604-9145 (DSN 664-9145), e-mail BFlynn@dodig.osd.mil or Mr. W. Andy Cooley at (303) 676-7393 (DSN 926-7393), e-mail WCooley@dodig.osd.mil. See Appendix E for the report distribution. The audit team members are listed inside the back cover.

A handwritten signature in black ink, reading "Robert J. Lieberman", is positioned above the typed name.

Robert J. Lieberman  
Assistant Inspector General  
for Auditing



## Office of the Inspector General, DoD

Report No. 99-004  
(Project No. 7FD-2037.02)

October 5, 1998

### Compilation of FY 1997 Air Force General Funds Consolidated Financial Statements at the Defense Finance and Accounting Service Denver Center

#### Executive Summary

**Introduction.** The Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, requires the Inspector General, DoD, or an appointee to audit the DoD financial statements. We delegated the audit of the FY 1997 Air Force General Funds Consolidated Financial Statements to the Air Force Audit Agency. The Defense Finance and Accounting Service Denver Center maintained accounting records and prepared the FY 1997 financial statements for the Air Force. More than \$343 billion in total assets was reported at year's end in these statements, and total revenues for the year exceeded \$64 billion. The Air Force Audit Agency disclaimed an opinion on these statements. Additionally, although the Office of Management and Budget does not require budgetary resource reporting until FY 1998, the Air Force implemented the reporting requirements early and included the Statement of Budgetary Resources in the FY 1997 Consolidated Financial Statements. Since the Air Force Audit Agency has not completed sufficient audit work to determine whether the Statement of Budgetary Resources is fairly presented, our compilation review of this statement continues. The Defense Finance and Accounting Service Denver Center compiles financial data and prepares financial statements for both the Air Force General Funds and Working Capital Funds. Our audit focused on the processing of financial data by the Defense Finance and Accounting Service Denver Center to compile the FY 1997 Air Force General Funds Financial Statements.

**Audit Objectives.** The primary audit objective was to determine whether the Defense Finance and Accounting Service Denver Center consistently and accurately compiled financial data from field activities and other sources for the financial statements of the Air Force General Funds. Additionally, we reviewed internal controls and compliance with laws and regulations related to the objectives. We also reviewed the adequacy of the management control program as it applied to the audit objective. Other objectives related to the oversight of the Air Force Audit Agency were covered in a separate audit report.

**Audit Results.** Although significant financial reporting challenges remained, the Defense Finance and Accounting Service Denver Center completed corrective actions on 12 of 22 prior recommendations made by the Inspector General, DoD, to improve the process of compiling Air Force financial statements. See Appendix C for details of the recommendations for which completed corrective actions were still lacking.

Subject to the scope limitations discussed in Appendix A, we determined that the Defense Finance and Accounting Service Denver Center accurately and consistently compiled the data for presentation on the financial statements. However, we noted that the Defense Finance and Accounting Service Denver Center adjusted financial data in the Chief Financial Officers Reporting System, Status of Funds, Command On-Line Accounting and Reporting System, and General Funds General Ledger system without appropriate management oversight. As a result, Defense Finance and Accounting Service Denver Center oversight of adjustments made to financial data reported in the FY 1997 Air Force General Funds Financial Statements was inadequate in some instances and excessive in others. Although no material errors were disclosed, these control weaknesses exposed the financial statement compilation process to increased risk of material misstatements, which may affect future financial statements. See Part I for a complete discussion of the finding. See Appendix A, Audit Process, for details of the review of the management control program.

**Summary of Recommendations.** We recommend that the Director, Directorate of Departmental Accounting, Defense Finance and Accounting Service Denver Center, establish written criteria for approving journal vouchers. The criteria should apply to all input and correcting adjustments and should provide for the establishment, maintenance, and distribution of a list of operating location managers authorized to request changes to certified data reported by each operating location.

**Management Comments and Audit Response.** The Defense Finance and Accounting Service did not respond to a draft of this report, issued August 28, 1998. We request that the Defense Finance and Accounting Service provide comments on the final report by October 30, 1998.

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## **Part I - Audit Results**

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## Audit Background

**Audit Requirement.** Public Law 101-576, the Chief Financial Officers Act of 1990 (the CFO Act), as amended by the Federal Financial Management Act of 1994, requires the Inspector General (IG), DoD, or an independent auditor appointed by the IG, DoD, to audit the financial statements of DoD reporting entities. We delegated the audit of the FY 1997 Air Force General Funds Consolidated Financial Statements to the Air Force Audit Agency (AFAA). The Defense Finance and Accounting Service (DFAS) Denver Center maintains records for the Department of the Air Force and prepared the FY 1997 Air Force General Funds Financial Statements from data submitted by the Air Force and other DoD organizations. More than \$343 billion in total assets was reported at year's end in these statements, and total revenues for the year exceeded \$64 billion. AFAA disclaimed an opinion on the FY 1997 statements. Additionally, although the Office of Management and Budget does not require budgetary resource reporting until FY 1998, the Air Force implemented the reporting requirements early and included the Statement of Budgetary Resources in the FY 1997 Consolidated Financial Statements. Since the AFAA has not completed sufficient audit work to determine whether the Statement of Budgetary Resources is fairly presented, our compilation review of this statement continues. Our audit focused on the processing of financial data by the DFAS Denver Center to compile the FY 1997 Air Force General Funds Financial Statements, but did not evaluate the validity of the data submitted for compilation. The DFAS Denver Center also compiles financial data and prepares financial statements for the Air Force Working Capital Funds, which were not included in this audit.

**Key Compilation Sources.** In compiling the FY 1997 Air Force General Funds Financial Statements, the DFAS Denver Center relied on data from external sources and key internal computer systems, as discussed below and illustrated in Appendix D.

**Status of Funds Database.** Each operating location (OPLOC) under the DFAS Denver Center electronically transmits budget data at the transaction level (certified by the OPLOC director) to the DFAS Denver Center through the Command On-Line Accounting and Reporting System (COARS). Data summaries of these detailed transactions are also provided by the OPLOCs to the DFAS Denver Center to ensure that all detailed transactions were accurately transmitted. Each unmatched summary-to-total-details condition is researched and corrected by the DFAS Denver Center. The budget data are then processed to the Status of Funds (SOF) database, which is part of the Department On-Line Accounting and Reporting System. Payment and collection transactions from the Merged Accountability and Fund Reporting (MAFR) system are also systematically included in the SOF database at the appropriation level. Budget data reported to the DFAS Denver Center, including subsequent modifications requested by the OPLOCs, are then processed to the CFO Reporting System for compilation into the Air Force General Funds financial statements. An automated interface is used to transfer data from the SOF to the CFO Reporting System.

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**Air Force General Funds General Ledger.** The Air Force General Funds General Ledger (GFGL) trial balances are another source for accounting information used in preparing the Air Force General Funds financial statements, such as the asset values reported for property, plant and equipment (PP&E). The GFGL trial balance is reviewed and adjusted by DFAS Denver Center accountants. Because no automated interface exists between the two systems, accounting information from the GFGL must be manually entered by the DFAS Denver Center into the CFO Reporting System.

**CFO Reporting System.** The CFO Reporting System compiles the Air Force General Funds financial statements using data obtained through its automated interface with the SOF and via manual data entry to record information extracted from the GFGL.

**DFAS Denver Center Adjustments.** Journal vouchers are used by the DFAS Denver Center to document the nature of and approval for adjustments made by accountants throughout the compilation process in the GFGL and CFO Reporting Systems and the nature of adjustments made in the SOF. This report refers to two types of adjustments.

**Input Adjustments.** Input adjustments are made only to reflect certified data actually reported by the OPLOCs, including subsequent revisions requested by authorized OPLOC staff. Also included in this category are any adjustments made to manually transfer data from one automated information system to another where an automated interface does not exist, such as between the GFGL and the CFO Reporting System. By their nature, input adjustments are low-risk and require minimal oversight by DFAS Denver Center managers.

**Correcting Adjustments.** These adjustments carry a higher risk than input adjustments because they are not supported by certified data reported by the OPLOCs. For example, center accountants make correcting adjustments in COARS, GFGL and the CFO Reporting System based on audit recommendations, DFAS guidance, and for other reasons. Thus, these adjustments require greater oversight by DFAS Denver Center managers.

## **Audit Objectives**

The primary audit objective was to determine whether the DFAS Denver Center consistently and accurately compiled financial data from field activities and other sources for the financial statements of the Air Force General Funds. We also reviewed internal controls and compliance with laws and regulations related to the objectives. We reviewed the adequacy of the management control program as it applied to the other stated audit objective. See Appendix A for a discussion of the scope and methodology and the results of our review of the management control program. See Appendix B for prior audits and other reviews and Appendix C for a discussion of recommendations from prior audits that have not been implemented.

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Other objectives related to the oversight of the Air Force Audit Agency were covered in Report No. 98-107, "Inspector General, DoD, Oversight of the Air Force Audit Agency Audit of the FY 1997 Air Force General Funds Financial Statements," April 7, 1998.

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## Adjustments To Financial Data

The DFAS Denver Center adjusted financial data in the CFO Reporting System, SOF, COARS, and GFGL without appropriate management oversight because:

- procedures for the CFO Reporting System were not followed in some instances and did not distinguish between input adjustments and correcting adjustments,
- no procedures had been established to require management oversight of journal voucher adjustments made in the SOF and GFGL, and
- no automated controls were in place to preclude accountants making undocumented SOF journal voucher adjustments.

As a result, the DFAS Denver Center oversight of adjustments made to financial data reported in the FY 1997 Air Force General Funds Financial Statements was inadequate in some instances and excessive in others. Although no material errors were disclosed, these control weaknesses exposed the financial statement compilation process to potential material misstatements.

## Approval Criteria

In FY 1997, the DFAS Denver Center issued an e-mail establishing managerial levels for the review and approval of journal voucher adjustments in the CFO Reporting System based on the dollar amount of the adjustment. These approval criteria, detailed in Table 1, applied equally to input adjustments and correcting adjustments.

**Table 1. Approval Criteria**

Journal Voucher Dollar Amount	Required Management Approval Level
Under \$0.1 billion	Level 1: Chief, CFO Branch
\$0.1 billion-\$1 billion	Level 2: Chief, Accounting and Reporting Division
\$1 billion-\$5 billion	Level 3: Director, Directorate of Departmental Accounting
\$5 billion-\$10 billion	Level 4: Deputy Director for Accounting
Over \$10 billion	Level 5: Director, DFAS Denver Center

No similar criteria had been established by the DFAS Denver Center for management review and approval of journal voucher adjustments made in the SOF or GFGL systems.

## **CFO Reporting System**

Of 20 journal vouchers examined, representing adjustments exceeding \$119 billion in the CFO Reporting System, 15 represented correcting adjustments, and 5 were input adjustments. Required approval was not obtained for 3 correcting adjustments, while an excessive level of management oversight was obtained on all 5 input adjustments.

**Required Approval.** The three correcting adjustments listed in Table 2 were made without the management approvals specified in Table 1.

**Table 2. Journal Vouchers Without Management Approval**

<u>Journal Voucher</u>	<u>Amount</u>	<u>Approved by</u>	<u>Required Approval</u>
G9700927	\$37.70 billion	Level 3	Level 5
G9700934	\$ 1.70 billion	Level 1	Level 3
G9700893	\$ 0.11 billion	Level 1	Level 2

CFO Branch personnel believed these three journal vouchers did not require approval above the Chief, CFO Branch. The \$37.7 billion adjustment was based on verbal directions from a DFAS manager to reclassify ammunition and operating materials from inventory to war reserve. The \$1.7 billion adjustment was based on an AFAA recommendation to record a liability for environmental cleanup costs. The third adjustment for \$114.3 million was calculated by a DFAS Denver Center accountant to adjust a receivable allowance account. None of these adjustments was requested nor supported by certified data provided by the OPLOCs.

**Excessive Approval Levels.** As required by the approval criteria in Table 1, all 5 input adjustments (voucher numbers G9700873, G9700875, G9700920, G9700923, and G9700937) were approved at a managerial level higher than the accountant's immediate supervisor. For example, journal voucher number G9700873 was approved by the Deputy Director, DFAS Denver Center, based on the \$41.6 billion amount of the adjustment. However, this journal voucher was made simply because of the lack of an automated interface between the GFGL system and the CFO Reporting System. Had such an interface existed, the financial data would have flowed from one computer system to the other without intervention or approval by any employee. Thus, having the accountant's immediate supervisor approve this journal voucher would have been more appropriate under the circumstances. The approval criteria for the CFO Reporting System should recognize the difference between input adjustments and the more sensitive correcting adjustments.

## **Status of Funds**

No management oversight was provided to the Report Change Memos prepared by center accountants to make journal voucher adjustments to SOF financial data.

In addition, DFAS Denver Center managers had no assurance that Report Change Memos were prepared to document every SOF change made by center accountants.

**Management Oversight.** DFAS Denver Center accountants prepared Report Change Memos to document journal voucher adjustments made to reconcile the SOF to the certified data initially reported by the OPLOCs and for subsequent changes requested by OPLOC staff. Supporting records for such certified data are maintained at the OPLOC, not at the DFAS Denver Center. Thus, the only support for the Report Change Memos prepared by accountants is the original certified data from the OPLOCs, plus copies of OPLOC e-mails or other documents requesting subsequent changes. The accountants did not have a list of personnel authorized by the OPLOC directors to request changes to certified OPLOC data.

These SOF journal voucher adjustments require minimal oversight because such input adjustments are made only to reflect certified data (including subsequent changes) actually reported by the OPLOCs. Combined with a list of OPLOC staff authorized to request SOF changes, approval of the Report Change Memos by an immediate supervisor should provide reasonable control over such SOF adjustments. However, the DFAS Denver Center did not have an internal procedure requiring approval of the Report Change Memos by the accountant's immediate supervisor. Furthermore, center procedures did not require OPLOC directors to provide center accountants with a list of OPLOC staff authorized to request changes to SOF data. As a result, there was no assurance that SOF journal voucher adjustments made by the DFAS Denver Center accountants in response to requests by OPLOC personnel were authorized. In addition, the absence of minimal managerial oversight over SOF adjustments made by Report Change Memos increases the possibility of error.

**Controls Over SOF Changes.** DFAS Denver Center managers had no means of verifying that Report Change Memos were prepared to document every SOF change made by center accountants. By comparing the SOF inputs and outputs, the audit identified one SOF change that was not supported by a Report Change Memo. Although not of material effect, in making this undocumented change, the accountant made an error in logic that overstated FY 1997 Air Force General Funds revenues by more than \$38 million. The SOF database at the end of each month overlays and erases the SOF database for the preceding month. Thus, the \$38 million error that overstated Air Force General Funds revenues by \$38 million as of September 30, 1997, would have been corrected when overlaid by the SOF database as of October 31, 1997. However, because the September 30, 1997 SOF data was used in preparing year-end financial statements, that error or similar errors could have materially affected the FY 1997 Air Force General Funds Financial Statements. There are no automated controls over SOF journal voucher adjustments made by accountants each month that would record or otherwise preclude such adjustments from being made without the knowledge and approval of DFAS managers. Thus, material SOF journal voucher adjustments could be made to the Air Force financial statements without the knowledge and oversight of DFAS managers. When informed of this problem, DFAS Denver Center immediately adopted the audit technique of comparing the SOF inputs and outputs

## **Adjustments to Financial Data**

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to verify that all SOF journal voucher adjustments were supported by Report Change Memos. Accordingly, no recommendation is being made, because this new management control should ensure that all SOF journal voucher adjustments are properly documented.

## **General Funds General Ledger System**

Inconsistent or no management oversight was given to input and correcting journal voucher adjustments made to PP&E; progress payments; and the values of operating materials and supplies reported in the GFGL, including COARS data inputs. As illustrated in Appendix D, inputs to the GFGL include field data from the COARS and other sources of PP&E data. Once recorded in GFGL, this data is later manually transferred to the CFO Reporting System via input adjustments.

**COARS Data Inputs to GFGL.** When COARS data are transferred to GFGL each quarter, the new COARS data input overlays and erases the data residing in GFGL, which represents data from the last COARS transfer plus department-level adjustments made by accountants in GFGL. Because all GFGL data will be erased, the transfer of COARS data required for preparing the Air Force financial statements is delayed as long as possible to maintain the integrity of the command-level system COARS. For example, COARS data for the fourth quarter of FY 1997 was not transferred to GFGL until late November 1997, when it was required for use by the DFAS Denver Center in preparing the first version of the FY 1997 Air Force General Funds Financial Statements.

**Journal Vouchers.** DFAS Denver Center accountants used two types of journal vouchers to adjust data recorded in COARS and GFGL. Before the COARS transfer to GFGL, accountants made command-level journal vouchers without any management oversight to document the changes they made to COARS data. Once COARS data were transferred to GFGL, the accountants used department-level journal vouchers to document adjustments made to GFGL, all of which were approved by the Chief, CFO Branch.

The only distinction between command- and department-level journal vouchers was the automated information system used to record the adjustment, as dictated when COARS data were transferred to GFGL. Management oversight was not provided to command-level journal vouchers, but all department-level vouchers were approved by the Chief, CFO Branch. As illustrated below, inconsistent levels of management oversight were given to the input and correcting adjustments made in COARS and GFGL via command- and department-level journal vouchers.

**Aircraft.** In November 1997, accountants made a command-level adjustment (voucher number 97-500003) to record a combination of an input and correcting adjustment to COARS aircraft and missile values. An input adjustment was made to record more than \$150 billion in aircraft and missile values obtained from a field organization report produced by the Equipment Inventory, Multiple Status and Utilization Reporting System (EIMSURS). The command-level adjustment also reflected a Correcting Adjustment to aircraft values reported by the EIMSURS report. That is, the command-level adjustment included a correction by an accountant to reduce the EIMSURS aircraft values by

\$48 million, based on information obtained from an undocumented General Accounting Office (GAO) report, plus an offsetting increase of more than \$170 million, based on revised aircraft unit costs obtained from a prior-year AFAA audit. However, in December 1997, the earlier command-level adjustment was partially reversed by a department-level adjustment approved by the Chief, CFO Branch. That correcting adjustment had to be made because it was later determined that the earlier unit cost adjustment for \$170 million was unnecessary.

**Missiles.** A correcting adjustment was made by a command-level journal voucher (voucher number 97-500010) to increase PP&E values reported by over \$1 billion to record missile motors identified as having been omitted from the EIMSURS report. In January 1998, however, a department-level adjustment (voucher number 98-023) was approved by the Chief, CFO Branch, to reduce the PP&E value reported by GFGL by \$1.7 billion when a determination was made that the missile motors had already been included in the values reported for completed missiles by the EIMSURS report.

**Munitions.** The Chief, CFO Branch, approved a department-level journal voucher in November 1997 to make an input adjustment (voucher number 98-001) to GFGL to record munitions valued at more than \$20 billion, which were identified in field reports. Had this information been available before the transfer of COARS data to GFGL, a command-level adjustment would have been made, which, as discussed above, would not have received any management oversight.

Inconsistent or no management oversight was given to input and correcting adjustments made to COARS and GFGL data because no procedure had been established, similar to that described in Table 1. Data recorded in COARS and GFGL are ultimately transferred to the CFO Reporting System. Thus, input and correcting adjustments made in COARS and GFGL via command- and department level journal vouchers should be subject to the same approval criteria as similar adjustments made in the CFO Reporting System.

## Summary

To improve oversight of the compilation process for Air Force financial statements, DFAS Denver Center should revise and establish operating procedures that provide consistent approval criteria for journal voucher adjustments made by DFAS Denver Center accountants to financial data recorded in the CFO Reporting System, SOF, COARS, and the Air Force GFGL. Such procedures should recognize the different levels of oversight required for input adjustments and the more sensitive correcting adjustments. Likewise, these procedures should include controls needed to ensure that DFAS Denver Center accountants change certified field data only in response to requests by authorized OPLOC or other field personnel.

## **Recommendations for Corrective Action**

We recommend that the Director, Directorate of Departmental Accounting, Defense Finance and Accounting Service Denver Center, establish and provide accountants and managers with written criteria for approving journal vouchers that:

1. Appropriately distinguish between an input adjustments and a correcting adjustments.
2. Applies to input and correcting adjustments made to financial data recorded in the Chief Financial Officers Reporting System, Status of Funds, Command On-Line Accounting and Reporting System, and Air Force General Funds General Ledger System.
3. Provides for the establishment, maintenance, and distribution of a list of operating location managers who are authorized within specified dollar ranges to request changes to certified data reported by each operating location.

## **Management Comments Required**

The Defense Finance and Accounting Service did not comment on the draft report. We request that the Defense Finance and Accounting Service provide comments on the final report.

## **Part II - Additional Information**

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# Appendix A. Audit Process

## Scope and Methodology

We reviewed the process used by the DFAS Denver Center to compile financial data from Air Force field activities and other sources for inclusion in the FY 1997 Air Force Consolidated Financial Statements. Our audit focused on:

- the processing of budgetary data in the COARS and in the SOF, and
- the processing of PP&E (more than \$249 billion), progress payments (more than \$7 billion), and operating materials and supplies (more than \$38 billion) data in the GFGL.

Additionally, we evaluated the subsequent compilation of the financial data in the CFO Reporting System for presentation on the financial statements. To assess compliance with Office of Management and Budget (OMB) guidance, General Accounting Office standards, and DoD accounting policies, we reviewed adjustments made by DFAS Denver Center accountants, the importation of data into the CFO Reporting System, and the crosswalk of data to the financial statements. In addition, we identified recommendations from prior IG, DoD, audits at the DFAS Denver Center that affected the compilation of data for the FY 1997 financial statements.

**Limitations to Scope.** The scope of this audit was limited in the following respects.

**Auditor Opinion.** The objective of our audit was to evaluate whether the DFAS Denver Center fulfilled its responsibilities for preparing the Air Force financial statements. Accordingly, we did not render an opinion on the financial statements. We endorsed the AFAA disclaimer of opinion on the Air Force financial statements in its Report No. 97053009, "Opinion on Fiscal Year 1997 Air Force Consolidated Financial Statements," February 27, 1998. We did not evaluate the accuracy of data provided by Air Force field activities. The AFAA included this evaluation in its review.

**Other Financial Statements.** We did not evaluate the compilation procedures used by the DFAS Denver Center to prepare the Air Force Working Capital Fund Consolidated Financial Statements for FY 1997. Since the AFAA has not completed sufficient audit work to determine whether the Statement of Budgetary Resources is fairly presented, our compilation review of this statement continues.

**Audit Results.** The audit results were based on an analysis of financial data processed through COARS, SOF, GFGL, and the CFO Reporting System, subject to the following limitations. We evaluated the approval of adjustments to budgetary data in COARS and SOF; PP&E, progress payments, and operating

materials and supplies in GFGL; and financial data in the CFO Reporting System. We did not evaluate the validity of these data. Additionally, we did not evaluate the propriety of the posting of financial data to general ledger accounts during the importing of budgetary data into the CFO Reporting system. Finally, we did not evaluate the disbursement and collection data processed through MAFR.

**DoD-wide Corporate Level Government Performance and Results Act (GPRA) Goals.** In response to the GPRA, the Department of Defense has established 6 DoD-wide corporate level performance objectives and 14 goals for meeting these objectives. This report pertains to achievement of the following objective and goal.

**Objective:** Fundamentally reengineer the Department and achieve a 21st century infrastructure. **Goal:** Reduce costs while maintaining required military capabilities across all DoD mission areas. **(DoD-6)**

**DoD Functional Area Reform Goals.** Most major DoD functional areas have also established performance improvement reform objectives and goals. This report pertains to achievement of the following functional area objectives and goals.

**Financial Management Functional Area. Objective:** Strengthen internal controls. **Goal:** Improve compliance with the Federal Managers Financial Integrity Act (FMFIA). **(FM-5.3)**

**General Accounting Office High-Risk Area.** The GAO has identified several high-risk areas in the DoD. This report provides coverage of the Defense Financial Management high-risk area.

**Use of Computer-Processed Data.** To achieve the audit objectives, we relied extensively on computer-processed data in the COARS, SOF, GFGL, and the CFO Reporting System. The audit scope did not include evaluating the reliability of the data in these systems. As discussed in Appendix C, DFAS is enhancing the existing General Accounting and Finance System to provide reliable data for preparing Air Force General Funds financial statements.

**Audit Period, Standards, and Locations.** We performed this financial-related audit from August 1997 through August 1998 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the IG, DoD. We included tests of management controls considered necessary.

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

## Management Control Program

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

**Scope of Review of Management Control Program.** We reviewed the adequacy of the management controls over the preparation of financial statements and the DFAS Denver Center's self-evaluation of those controls. Specifically, we reviewed the management controls over the COARS, SOF, GFGL, and the CFO Reporting System to determine whether the systems were complete and auditable.

**Adequacy of Management Controls.** We identified material management control weaknesses at DFAS, as defined by DoD Directive 5010.38. Approval of adjustments made to financial data used in the preparation of the financial statements was not adequate to ensure the validity of the data presented on the financial statements. Specifically, adjustments to financial data during the compilation process were made without appropriate management oversight. The weakness did not materially affect the compilation of the FY 1997 Air Force Financial Statements, but may affect future statements. Implementing Recommendations 1, 2, and 3 will improve management controls over adjustments made to financial data, but will not correct the material weaknesses identified in prior audits. A copy of the report will be provided to the senior DFAS official responsible for management controls.

**Adequacy of Management's Self-Evaluation.** DFAS Denver Center officials identified the department-level operations as a part of five separate assessable units: CFO/Financial Statement Branch, FMFIA/CFO Branch, Status of Appropriations, Other Services Accountability, and Air Force Cash/Treasury Accountability. Risk assessments of these branches identified medium risk for all branches except the FMFIA/CFO Branch, which was assessed as low risk. Although management performed a self-evaluation, they did not identify and implement corrective actions for the specific material weakness identified.

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## **Appendix B. Summary of Prior Coverage**

The GAO; the IG, DoD; and the AFAA have issued numerous reports that identified weaknesses in the internal controls over the compilation of data used in the Air Force financial statements.

### **General Accounting Office**

Report No. AFMD-92-12 (OSD Case No. 8376-L), "Aggressive Actions Needed for Air Force to Meet Objectives of the CFO Act," February 19, 1992.

### **Inspector General, DoD**

Report No. 98-054, "Compilation of FY 1996 Air Force Consolidated Financial Statements at the Defense Finance and Accounting Service Denver Center," January 23, 1998.

Report No. 97-057, "Compilation of FY 1995 Air Force Consolidated Financial Statements at the Defense Finance and Accounting Service Denver Center," December 27, 1996.

Report No. 95-301, "Major Deficiencies Preventing Auditors From Rendering Audit Opinions on DoD General Fund Financial Statements," August 29, 1995.

Report No. 95-264, "Defense Finance and Accounting Service Work on the Air Force FY 1994 Financial Statements," June 29, 1995.

Report No. 95-067, "Defense Finance and Accounting Service Work on the Air Force FY 1993 Financial Statements," December 30, 1994.

Report No. 94-073, "Defense Finance and Accounting Service Work on the Air Force FY 1992 Financial Statements," March 31, 1994.

## **Air Force Audit Agency**

Project No. 97053009, "Opinion on Fiscal Year 1997 Air Force Consolidated Financial Statements," February 27, 1998.

Project No. 96053001, "Opinion on Fiscal Year 1996 Air Force Consolidated Financial Statements," March 1, 1997.

Project No. 95053001, "Opinion on Fiscal Year 1995 Air Force Consolidated Financial Statements," March 1, 1996.

Project No. 945053001, "Opinion on Fiscal Year 1994 Air Force Consolidated Financial Statements," March 1, 1995.

Project No. 94053022, "Opinion on Fiscal Year 1993 Air Force Consolidated Financial Statements," June 30, 1994.

Project No. 92053011, "Opinion on FY 1992 Air Force Consolidated Financial Statements," June 29, 1993.

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## Appendix C. Financial Management Challenges

### Previously Reported Issues

Of the 22 IG, DoD, audit recommendations open or issued after October 1, 1995, the DFAS Denver Center completed corrective action on 12. However, despite the progress made by Headquarters, DFAS, and the DFAS Denver Center, management still faced significant challenges in responding to the remaining 10 recommendations, which affected the compilation of data for the FY 1997 Air Force Consolidated Financial Statements. Included in those issues were problems related to:

- financial accounting systems, and
- the MAFR system.

Although Headquarters, DFAS, and the DFAS Denver Center had begun corrective action on all issues, the problems still existed because several of the corrective actions would not be completed before December 1999. As a result, we could not adequately evaluate the accuracy of data included in the FY 1997 Air Force Consolidated Financial Statements. Furthermore, future financial statement audits will be similarly affected as long as the problems exist.

### System Improvements

**Financial Management Operations.** DoD has emphasized long-term efforts to improve and standardize its financial management operations, but many of the benefits of those efforts will not be realized for several years. To correct accounting system deficiencies and to reduce the number of DoD accounting systems, in December 1993, DFAS established the General Funds Accounting System Improvement Plan.<sup>7</sup> Under the plan, in November 1995, the DFAS Denver Center began exploring and developing the General Ledger/Funds Control system. The overall goal of the General Ledger/Funds

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<sup>7</sup>For details of the plan, see IG, DoD, Report No. 96-180, "The General Fund Interim Migratory Accounting Strategy," June 26, 1996.

## **Appendix C. Financial Management Challenges**

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Control system was to integrate the production of accurate and timely financial statements and reports. Among other objectives, the General Ledger/Funds Control system was expected to:

- provide for a transaction-driven general ledger that complies with Federal regulations;
- incorporate the budget and accounting classification code; and
- bring accounting systems into conformance with generally accepted accounting principles.

In July 1996, however, the Under Secretary of Defense (Comptroller) directed DFAS to develop the Corps of Engineers Financial Management System, renamed Defense Joint Accounting System (DJAS), as the general funds accounting migratory system for customers of the DFAS Denver Center. That decision was based on a DFAS Denver Center determination that DJAS presented a viable option to satisfy the general funds accounting requirements of the DFAS Denver Center customers. However, the DJAS application for the Air Force General Funds was terminated in favor of enhancing the existing General Accounting and Finance System. The enhancement of GAFS affects the following issues, which are discussed below: the lack of a transaction-driven general ledger and a uniform chart of accounts; the use of budgetary data in proprietary accounts; the inability to differentiate between Government-furnished material and contractor-acquired material; and the inability to reconcile differences between the U.S. Treasury account balances and Air Force base-level accounts.

**Audit Followup.** Through its internal review function, the DFAS Denver Center monitors the status of corrective actions taken in response to prior audit recommendations and issues periodic status reports to DFAS. The DFAS Denver Center reported to the IG, DoD, that corrective actions were not complete on 10 prior audit recommendations made to fix problems with accounting systems and other issues. As discussed below, these problems affected our ability to evaluate the accuracy of data reported in the FY 1997 Air Force Consolidated Financial Statements.

### **Financial Accounting System Issues**

**Transaction-Driven General Ledger.** The DFAS Denver Center did not have a double-entry, transaction-driven general ledger system for preparing the Air Force consolidated financial statements. Without such a general ledger, the DFAS Denver Center could not prepare meaningful financial statements that met DoD accounting requirements. Report No. 94-073 recommended that the DFAS Denver Center develop and implement an integrated, double-entry, transaction-driven, general ledger system for preparing the Air Force financial statements.

**Uniform Chart of Accounts.** The DFAS Denver Center did not use the DoD Uniform Chart of Accounts, as required by DoD 7220.9-M, the "DoD Accounting Manual," October 1983. The Uniform Chart of Accounts is intended to

standardize DoD accounting and meet basic reporting requirements for Federal financial statements and budgets. Instead, the DFAS Denver Center used the Air Force Chart of Accounts, which did not have the same account structure and could not be reconciled to the DoD Uniform Chart of Accounts. The DFAS Denver Center's use of the Air Force chart of accounts did not allow reconciliation of budgetary data to proprietary accounting data, which contributed to the unreliability of the data used in preparing the Air Force financial statements. IG, DoD, Report No. 94-073 recommended that the DFAS Denver Center implement the DoD Uniform Chart of Accounts. With the Federal Financial Management Improvement Act of 1996, the DFAS Denver Center was required to implement the United States Standard General Ledger at the transaction level.

**Military Pay Data.** Military pay data reported in the Air Force consolidated financial statements were inaccurate because of year-end timing differences. The DFAS Denver Center improperly reported military separation pay in the year after it was earned. Also, the Summary of Military Pay Obligations system, used to report military pay activity, was cut off prematurely before the end of the fiscal year. Thus, payroll expenses that should have been reported in one year were improperly reported the next year. IG, DoD, Report No. 94-073 recommended that the DFAS Denver Center establish procedures to adjust for year-end separation pay and other timing differences. DFAS Denver Center managers are working to change the military pay system to provide estimates of the amounts attributable to the timing differences so that accounting personnel can manually adjust the Air Force financial statements. The DFAS Denver Center also plans to revise operating instructions to ensure that financial statements reflect the required adjustments. Those corrective actions are scheduled to be completed in FY 1998.

**Use of Budgetary Data.** We could not verify accounts payable reported on the Air Force Statement of Financial Position because the DFAS Denver Center used questionable budgetary data instead of general ledger data. The budgetary data may have included duplicate amounts. IG, DoD, Report No. 94-073 recommended that the DFAS Denver Center use general ledger data instead of budgetary data to prepare the financial statements.

**Government-Furnished Material and Contractor-Acquired Material.** In preparing the Air Force Consolidated Financial Statements, the DFAS Denver Center did not properly account for Government-furnished material and contractor-acquired material. The DFAS Denver Center guidance on the reporting of those materials in the Air Force Consolidated Financial Statements was inconsistent with DoD and Air Force regulations. IG, DoD, Report No. 94-073 recommended that the DFAS Denver Center develop and implement changes in internal guidance to conform to these regulations. However, the DFAS Denver Center does not have a system that can differentiate between Government-furnished material and contractor-acquired material with supporting documentation.

**Fund Balance With Treasury.** DFAS Denver Center personnel did not reconcile differences between the U.S. Treasury account balances and Air Force base-level accounts, as required by OMB and DoD regulations. OMB Circular No. A-34, "Instructions on Budget Execution," December 1995, requires that Fund Balance

## Appendix C. Financial Management Challenges

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With Treasury on the financial statements be supported by the entity's accounting records and be reconciled to the corresponding accounts reported on the U.S. Treasury's end-of-period balances. The "DoD Accounting Manual" requires that amounts reported by the U.S. Treasury be verified against data in the agency's records. DFAS Denver Center personnel made unsupported adjustments to the "Report on Budget Execution" to force agreement with the U.S. Treasury. IG, DoD, Report No. 94-073 recommended that the DFAS Denver Center reconcile the Air Force accounting records to Fund Balance With Treasury and limit adjustments to valid changes supported by documentation. DFAS Denver Center personnel now manually reconcile their balances with the U.S. Treasury every month, and all adjustments, except for undistributed amounts, are supported by documentation.

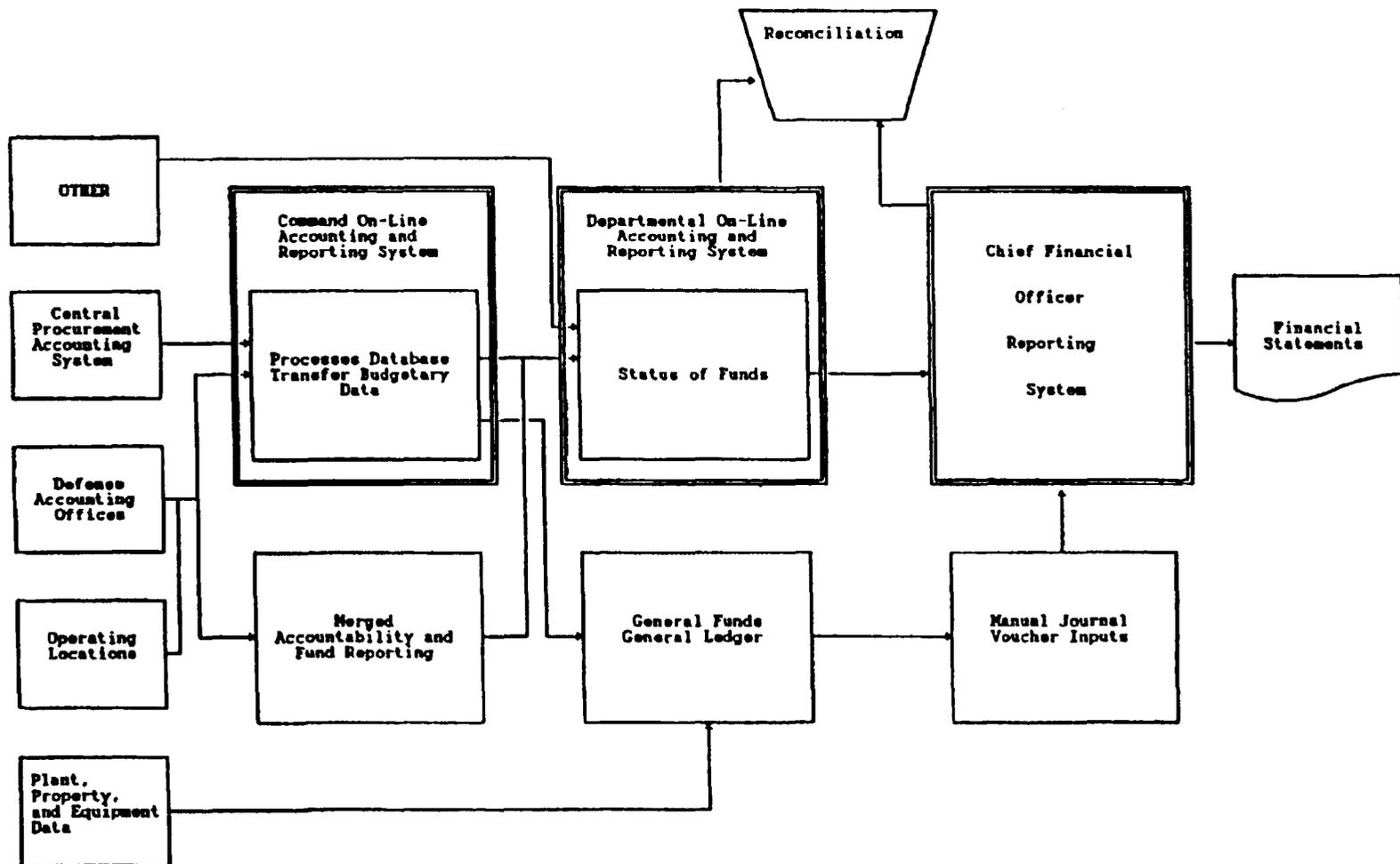
### MAFR System Issues

Problems related to the MAFR system's internal controls over reconciling account balances and maintaining an adequate audit trail were identified in prior IG, DoD, reports.

**MAFR System Reconciliations.** In preparing the FY 1992 Air Force consolidated financial statements, the DFAS Denver Center did not reconcile out-of-balance cash disbursements and receipts in the MAFR system. The MAFR system accounts for all cash transactions affecting the Air Force and provides consolidated cash accountability and reporting. Air Force Regulation 177-101, "General Finance and Accounting Systems at Base Level," February 15, 1991, requires the DFAS Denver Center to reconcile the cumulative dollar amounts at the department level to the monthly MAFR packages submitted by each Air Force disbursing station. If an out-of-balance condition exists, DFAS Denver Center personnel are to establish the source of the condition, require a reconciliation of data, and correct the out-of-balance condition. Report No. 94-073 recommended that the DFAS Denver Center perform MAFR system reconciliations and make appropriate corrections. To correct this situation, the DFAS Denver Center enhanced the manual internal controls in the MAFR system and requested a system change to automate those reconciliations. The change was expected to be completed by September 1998.

**MAFR Audit Trails.** The MAFR system did not maintain an adequate audit trail or transaction histories for transactions originating at the DFAS Denver Center. As a result, DFAS Denver Center managers could not identify all the adjustments to the MAFR system database and, therefore, could not verify that such adjustments were adequately supported or properly recorded. Before the prior audit was completed in February 1995, the DFAS Denver Center included the requirement for audit trails in the specifications for the Defense Cash Management System, which was expected to replace the MAFR system before FY 1999.

## Appendix D. DFAS Denver Center Compilation Process for Air Force General Funds



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## **Appendix E. Report Distribution**

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

Under Secretary of Defense (Comptroller)  
Deputy Chief Financial Officer  
Director, Accounting Policy  
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

### **Other Defense Organizations**

Director, Defense Contract Audit Agency  
Director, Defense Finance and Accounting Service  
Director, Finance Deputate, Defense Finance and Accounting Service  
Director, Defense Finance and Accounting Service Denver Center  
Chief, Internal Review Office  
Director, Defense Logistics Agency  
Director, National Security Agency  
Inspector General, National Security Agency  
Inspector General, Defense Intelligence Agency

## **Non-Defense Federal Organizations**

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

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

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



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