

Audit



Report

RELIABILITY OF THE MILITARY DEPARTMENTS REAL
PROPERTY DATABASES FOR EXISTENCE AND COMPLETENESS

Report No. 99-243

August 27, 1999

Office of the Inspector General
Department of Defense

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Acronyms

AAA	Army Audit Agency
CEFMS	Corps of Engineers Financial Management System
NAS	Naval Audit Service
REMIS	Real Estate Management Information System



INSPECTOR GENERAL
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August 27, 1999

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)

SUBJECT: Audit Report on Reliability of the Military Departments Real Property
Databases for Existence and Completeness (Report No. 99-243)

We are providing this audit report for review and comment. We performed the audit to support the requirements of the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994. We considered management comments on a draft of this report when preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. As a result of management comments, we revised the recommendation to clarify our intention. Therefore, we request that you provide additional comments to the final report by October 27, 1999.

Questions on the audit should be directed to Mr. David F. Vincent at (703) 604-9110 (DSN 664-9110) (dvincent@dodig.osd.mil) or Ms. Barbara A. Sauls at (703) 604-9129 (DSN 664-9129) (bsauls@dodig.osd.mil). See Appendix C for the report distribution. The audit team members are listed inside the back cover.

A handwritten signature in cursive script, 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. 99-243
(Project No. 9FH-3001)

August 27, 1999

Reliability of the Military Departments Real Property Databases for Existence and Completeness

Executive Summary

Introduction. This audit was performed to support the requirements of the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994. Because DoD real property represents 45 percent of the Federal Government's real property assets, accurate reporting of the real property part of the property, plant, and equipment account is critical to achieving a favorable audit opinion. The Office of Management and Budget; the General Accounting Office; the Under Secretary of Defense (Comptroller); and the Inspector General, DoD, jointly developed DoD implementation strategies to accomplish those goals. The first implementation strategy addressed the need to conduct audit tests for existence (verify that a record in the database has a corresponding item), completeness (verify that an observed item has a record in the database), and accuracy (check for supporting documentation) of the Military Departments' real property databases. The second implementation strategy addressed the issue of valuing general property, plant, and equipment in DoD. Specifically, if the databases did not contain cost data, or did not have supporting documentation for the cost data entered on the property records, an appropriate methodology would need to be developed to estimate the Government cost to acquire, construct, or improve real property.

Objectives. The overall audit objective was to determine whether the real property databases in the Military Departments were reliable for existence and completeness. In addition, the Military Department audit agencies tested the accuracy of the key data elements in the real property databases and the availability of supporting documentation for cost values assigned to the real property assets. Internal controls, compliance with laws and regulations, and the management control program will be assessed during a related audit on additions and deletions of real property assets.

Results. Statistical sample testing for existence showed that real property databases, with a reported value of \$71.2 billion, contained sufficiently accurate inventories of real property with individual reported values of greater than \$100,000. Sampling results showed that, at the 90 percent confidence level, the Military Departments had less than a 5 percent error rate for unaccounted items. However, Air Force items with individual reported values of less than \$100,000 had an estimated error rate of as much as 8.62 percent at the 90 percent confidence level. As a result, if the capitalization threshold were lowered to less than \$100,000, the Air Force real property databases may not contain records for all properties valued at less than \$100,000 and could be

considered unreliable for existence. Although not statistically demonstrable, the Army had one or more completeness errors at half of the locations tested. Test results on the accuracy of the key data elements, such as cost and ownership, in the real property databases were inconclusive. The errors identified in the Army may indicate a problem with completeness of real property in the Army databases. Also, the key data elements needed to estimate the historical cost were not reliable to validate the real property reported on the DoD Agency-Wide financial statements for FY 1998 and may impact the Under Secretary of Defense (Comptroller) effort to value the real property.

Recommendation. We recommend that the Under Secretary of Defense (Comptroller) issue interim policy specifying the supporting documentation that the Military Departments should retain to validate the cost to acquire, construct, or improve real property. The policy change should be incorporated in the “Department of Defense Financial Management Regulation” upon its revision.

Management Comments. The Deputy Chief Financial Officer took exception to our recommending changes to the “Department of Defense Financial Management Regulation” [Regulation]. He stated that the office is in the process of revising the Regulation to specify the supporting documentation that should be retained to validate the cost to acquire, construct, or improve real property. Further, he stated there was a lack of specificity about problems encountered with key data elements in property records. Finally, he said that our comments about the potential effect of discrepancies in the Air Force property records if a change were made in the capitalization threshold were not informative or constructive.

Although not required to comment, the Army agreed with the report and issued policy to maintain records of capitalization and capital improvements of real property for the lifetime of all facilities. The complete text of the responses is at the Management Comments section. The comments are summarized and discussed in the Finding section of the report.

Audit Response. The comments from the Deputy Chief Financial Officer were nonresponsive. A revision to the Regulation generally takes months to finalize and in the meantime, the condition remains uncorrected. Guidance in the property, plant, and equipment area is crucial to correct documentation problems. We revised our draft report recommendation to request that the Under Secretary issue interim guidance specifying the supporting documentation that should be retained to validate the cost to acquire, construct, or improve real property. The Under Secretary should then incorporate the guidance in the “Department of Defense Financial Management Regulation,” in its next update. We reported problems with key data elements, at sufficient level of detail, to establish the need for improvements in policy guidance and to highlight awareness of the challenges that must be overcome to appraise the value of DoD real property. Our comments about the probable effect of capitalization threshold changes were necessary to establish awareness of a problem that real property officials must address.

We request the Under Secretary of Defense (Comptroller) provide comments on the revised recommendation by October 27, 1999.

Table of Contents

Executive Summary	i
Introduction	
Background	1
Objectives	2
Finding	
Accuracy of the Military Departments' Real Property Databases	3
Appendixes	
A. Audit Process	
Scope and Methodology	12
B. Summary of Prior Coverage	15
C. Report Distribution	17
Management Comments	
Under Secretary of Defense (Comptroller) Comments	19
Department of the Army Comments	21

Background

This audit was performed to support the requirements of the Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994. On May 15, 1998, the Secretary of Defense issued a memorandum, "Department of Defense Financial Business Practices Reform," which stated a commitment to the Clinton Administration's goal of obtaining an unqualified audit opinion on the FY 1999 Consolidated Financial Statements of the Federal Government. Because DoD real property, reported in FY 1998 at \$71.2 billion, represents 45 percent of the Federal Government's property, plant, and equipment, accurate reporting of the real property portion of the property, plant, and equipment account is critical to achieving the Clinton Administration's goal.

The Office of Management and Budget; the General Accounting Office; the Under Secretary of Defense (Comptroller); and the Inspector General, DoD, jointly developed DoD implementation strategies. The first implementation strategy addressed the need to conduct audit tests for existence (verify that a record in the database has a corresponding item), completeness (verify that an observed item has a record in the database), and accuracy (check for supporting documentation) of the Military Departments' real property databases. The tests were designed to validate the real property databases. The second implementation strategy addressed the issue of valuing general property, plant, and equipment in DoD. Specifically, if the databases did not contain cost data, or did not have supporting documentation for the cost data entered on the property records, an appropriate methodology would need to be developed to estimate the Government cost to acquire, construct, or improve real property. In support of the management effort, the Under Secretary of Defense (Comptroller) contracted with an independent certified public accounting firm to assist in the real property valuation effort.

Both the Under Secretary of Defense (Comptroller) and the financial managers of the Military Departments were aware of the many problems with accounting for property, plant, and equipment. Prior audits identified the internal control weaknesses associated with the account such as the inability to validate the account balances. The DoD Annual Statement of Assurance for FY 1998 addressed the system problems associated with information feeding from nonfinancial systems into the financial statements.

The Army Audit Agency, the Naval Audit Service, and the Air Force Audit Agency were tasked to test for existence, completeness, and accuracy of the key data elements in the Military Departments' real property databases. Each audit agency developed a sampling plan to test the databases within its Military Department. The Inspector General, DoD, reviewed and approved the sampling plans. In addition, the General Accounting Office and the Inspector General,

DoD, performed audit work with the audit agencies. Each audit agency issued a report on the accuracy of the real property databases for its Military Department. This report summarizes those reports.

Objectives

The overall audit objective was to determine whether the real property databases in the Military Departments were reliable for existence and completeness. In addition, the Military Department audit agencies tested the accuracy of the key data elements in the real property databases and the availability of supporting documentation for cost values assigned to the real property assets. Internal controls, compliance with laws and regulations, and the management control program will be assessed during a related audit on the additions and deletions of real property assets. See Appendix A for a discussion of the audit scope and methodology. See Appendix B for a summary of prior coverage related to the audit objectives.

Accuracy of the Military Departments' Real Property Databases

Statistical sample testing for existence showed that real property databases, with a reported value of \$71.2 billion, contained reasonably accurate inventories of real property with individual reported values of greater than \$100,000. However, Air Force items with individual reported values of less than \$100,000 had an estimated error rate of as much as 8.62 percent. Although not statistically demonstrable, the Army had one or more completeness errors at half of the locations tested. Test results on the accuracy of the key data elements, such as cost and ownership, in the real property databases were inconclusive.

- The sampling results showed that, at the 90 percent confidence level, the Military Departments had less than a 5 percent error rate for unaccounted items.
- The Air Force had existence errors for items with individual reported values of less than \$100,000 primarily because real property officials did not receive the paperwork to remove facilities from the databases.
- The completeness errors in the Army stemmed partly from a system conversion in the Army Corps of Engineers.
- The test results on the accuracy of key data elements were inconclusive because DoD policy guidelines did not specify or define documentation for the Military Departments to maintain for the key data elements, and the documentation was inconsistent.

As a result, the inventories for items with values greater than \$100,000 were sufficiently reliable, in terms of indicating item existence, to be used for financial reporting purposes. However, if the capitalization threshold* were lowered to less than \$100,000, the Air Force inventory for items below \$100,000 may not contain records for all properties and could be considered unreliable for existence. The errors identified in the Army may indicate a problem with completeness of real property in the Army databases. Also, the key data elements for estimating the historical cost were not reliable to validate the real property reported on the DoD Agency-Wide financial statements for FY 1998 and may impact the Under Secretary of Defense (Comptroller) effort to value the real property.

*The capitalization threshold is the minimum acquisition or capital improvement cost of property that should be reported on the financial statements. At the time of this audit, the DoD capitalization threshold was \$100,000. If the capitalization threshold is lowered, more items will be reported on the financial statements. Lowering the threshold would increase the need for better accountability of items at that lower threshold.

Military Departments' Real Property Databases

Within DoD, each Military Department uses its own systems to record the additions, deletions, or modifications of real property assets. The Army uses a number of systems to maintain the real property databases, including the Integrated Facilities System. The Army Corps of Engineers uses the Real Estate Management Information System and the Corps of Engineers Financial Management System. The Navy uses the Navy Facility Assets Data Base. The Air Force uses the Interim Work Information Management System. The values assigned to the assets in those databases were obtained from DD Forms 1354, "Transfer and Acceptance of Real Property"; original or recently generated property record cards; or various other sources.

DoD Instruction 4165.14, "Inventory of Military Real Property," December 21, 1966, through change 4, August 25, 1977, states that the inventory is the basic source of information for reports of status, cost, maintenance, and management of real property. The instruction requires that the Military Departments prepare summary reports annually. In addition, the Military Departments must maintain an individual real property record for every item of real property that they own, lease, or otherwise acquire and control. The instruction identifies the basic identifying information that the property records should contain such as the date acquired, condition, year built, ownership, and cost of owned construction.

DoD Financial Management Regulation, volume 4, chapter 6, "Fixed Assets," January 1995, requires fixed asset accounts to bring the acquisition cost of DoD property under financial control. Section 060212 of the regulation states that entries recording transactions in accounting system general ledger accounts and the supporting subsidiary property records must be supported by source documents that capture acquisition costs and capital improvements. The regulation requires that DoD Components maintain source documents to enable periodic independent verification of the accuracy of accounting records through a periodic physical count and reconciliation between the subsidiary property records and the general ledger. Physical inventories are required every 5 years. If the inventories are completed as required and the reconciliations between the accounting records and the property records are made, then the completeness of the real property databases would be more certain. We considered an error rate of 5 percent or greater to be unacceptable and an indication that a database could not be relied on for existence.

Testing the Real Property Databases for Item Existence

The real property databases in the Military Departments were reliable for existence. The auditors used statistical sampling to test the databases for existence errors. The auditors considered it a critical error for existence when they could not verify the item sampled from the real property database. To accept the real property databases for existence, the upper bound of the error rate had to be less than 5 percent at the 90 percent confidence level. In addition, to be reported on the financial statements, the real property assets had to be reported at a value of greater than the capitalization threshold of \$100,000. The following table summarizes the results of testing the real property databases for existence.

Results of Existence Testing in the Military Departments

<u>Real Property Database</u>	<u>Percent Existence Errors¹</u>
Army	4.23
Navy ²	3.84
Air Force ²	4.59

¹ At the 90 percent confidence level.

² Individual reported values of greater than \$100,000.

The errors identified did not have a major impact on the real property databases. However, the portion of the Air Force real property database with individual reported values of less than \$100,000 had an 8.62 percent error rate at the 90 percent confidence level. The higher error rate may be an indication that less attention is provided to items with a reported value of less than \$100,000. As a result, the reliability of the Air Force databases may be an issue if the capitalization threshold is lowered to less than \$100,000.

Army Results. Tests at 62 locations Army-wide showed that Army databases could be relied on to reflect item existence. Most existence problems were with support facilities such as parking lots and utilities. Other problems involved the conversion of properties. For example, at Fort Bragg, a wash platform was paved over and converted to a parking lot. Real property personnel did not know of the conversion and consequently did not have the wash platform removed from the database. Overall, the Army real property database contained no more than 4.23 percent existence errors at the 90 percent confidence level. Therefore, the Army Audit Agency (AAA) concluded that the Army real property databases reliably indicated item existence, and we agree.

Navy Results. In the Navy, the Navy Facility Assets Data Base was used to capture the data on real property assets. The Naval Audit Service (NAS) divided the September 30, 1997, real property database into two parts: property reported at a cost of greater than \$100,000 and property reported at a cost of less than \$100,000. The portion of the Navy real property database with individual reported values of greater than \$100,000 contained no more than 3.84 percent existence errors at the 90 percent confidence level. The NAS determined that real property managers generally complied with applicable laws and regulations but noted minor internal control problems. The errors that were identified for individual reported values of greater than \$100,000 were the results of organizations that could not identify where parcels of land shown in the Navy Facility Assets Data Base were actually located. In addition, buildings were dismantled and moved to non-Department-of-the-Navy locations, and demolished buildings were not removed from the database. Another problem

was at the Naval Air Station Sigonella, Italy. A \$7 million building was included in the database in anticipation of construction, but the construction never took place. Real property officials removed the building from the database.

Of the items sampled from the portion of the Navy real property database with individual reported values of less than \$100,000, NAS identified 32 existence errors. The NAS judgmentally considered that portion of the Navy real property database to be sufficiently accurate based on the results. Consequently, NAS concluded that the real property database for the Navy reliably reflected item existence, and we agree.

Air Force Results. The Air Force real property databases for facilities reported at greater than \$100,000 were reasonably accurate and could be considered reliable for reporting item existence. They had no more than a 4.59 percent existence error in the population at the 90 percent confidence level. The errors occurred because the real property officials had not provided the required paperwork needed to remove three facilities that had been destroyed near the end of the fiscal year. For example, at Whiteman Air Force Base, two facilities were awaiting removal from the system since May and October 1997. As a result, the Air Force Audit Agency recommended that the real property officers adopt year-end procedures to remove destroyed facilities before complete paperwork is processed.

The Air Force Audit Agency selected another sample with individual reported values of less than \$100,000. The sample contained as much as 8.62 percent existence errors at the 90 percent confidence level. The errors occurred primarily because paperwork to remove facilities had not been provided to the real property officials. Although the real property databases reflected errors, those omitted items, with a reported value of less than \$100,000, did not affect the conclusions regarding the DoD real property databases. In addition, at the time of the audit, those omitted items would not be used to calculate the amount reported on the financial statements. However, if the threshold were lowered to less than \$100,000, and those items were omitted from the real property databases, the dollar value of those omitted items would not be included in the financial statements. The Air Force Audit Agency concluded that the real property database in the Air Force reliably reflected items for existence, and we agree.

Conclusions. We concur with the Military Department auditors' conclusions that, in testing for existence, the real property databases at the Military Departments were reliable for items reported at a value of greater than \$100,000. However, for items reported at a value of less than \$100,000 in the Air Force, the real property databases did not reliably reflect those items for existence. Real property officials did not provide the same level of attention to assets that were reported at a value of less than \$100,000 as assets with a reported value of greater than \$100,000. If the difference in the level of attention remains, the reliability of the real property databases in the Air Force could become an issue, if the capitalization threshold is set below \$100,000.

Testing the Real Property Databases for Completeness

To be considered a completeness error, the real property item selected for tracing back to the real property database would not be included in the real property database. To test completeness, the auditors judgmentally selected 10 items, if available, at each location where existence testing was performed and traced the selected items back to the real property database to verify that they were included. If an item was not recorded in the real property database, the auditors interviewed real property officials to determine ownership of the asset. If the asset was Military-Department owned or if the military component being tested had an interest in the asset (for example, a capital lease arrangement) but the asset was not recorded in the real property database, a completeness error was recorded. Each Military Department audit agency reported its results to the financial managers or organizations within its Military Department.

Army Results. At the 62 locations that AAA visited, half of the locations had one or more errors for completeness. Specifically, the problem with the completeness testing stemmed partly from the conversion from the Corps of Engineers Management Information System to the Corps of Engineers Financial Management System (CEFMS). The Corps of Engineers Management Information System did not have subsidiary ledgers for real property. The individual assets contained in the real property system, the Real Estate Management Information System (REMIS), supported the Corps of Engineers Management Information System general ledger accounts. In effect, REMIS was the subsidiary ledger for the Corps of Engineers Management Information System. According to the AAA, REMIS had, and still had at the time of this audit, all the individual real property asset information.

During the conversion process, the Corps of Engineers organizations did not completely load the CEFMS subsidiary ledger, the Asset Cost Table, with the individual assets from REMIS. Those omissions of real property affected the amounts of depreciation expense and accumulated depreciation that would be reported on the FY 1998 financial statements. Those omissions did not affect the amount reported as the cost of real property because during conversion, the amount that was in the Corps of Engineers Management Information System was bulk loaded to the CEFMS general ledger. When AAA used the Asset Cost Table as the database to audit, the real property assets that were not in the CEFMS Asset Cost Table were reported as completeness errors. However, according to AAA, those same real property assets were in the real property system REMIS. AAA identified the problem that the general ledger and subsidiary ledger (Asset Cost Table) were not in agreement during the FY 1997 audit of the Corps of Engineers financial statements. As a result, the Corps of Engineers began corrective action to add all of its assets from REMIS to the Asset Cost Table. The Corps of Engineers originally established March 31, 1999, as the deadline to have all assets loaded in the Asset Cost Table. Although the Corps of Engineers did not load all assets in the Asset Cost Table by the deadline, it had made progress.

Within other Army operations, AAA noted discrepancies when the real property databases did not include 48 of the 161 facilities located on the installations. For example, during an inventory at the 99th Army Reserve Center in Ripley,

West Virginia, real property officials identified six unrecorded assets. The AAA verified one or more completeness errors at 31 of 62 locations. Because the errors identified could not be statistically projected, AAA concluded that the errors only indicated a potential problem with the completeness of real property in the Army databases.

Navy Results. The NAS traced real property at 73 organizations where existence testing had been accomplished. The NAS judgmentally selected 523 buildings. Of the 523 buildings, 4 were not recorded in the Navy Facility Assets Data Base.

Air Force Results. The Air Force Audit Agency judgmentally sampled real property for tracing back to the real property database at 1,459 facilities and found 24 errors.

Conclusion. Although the Military Departments, and the Army in particular, had errors in completeness, we could not assess the reliability of the real property databases for completeness. The auditors judgmentally sampled items for completeness testing. Therefore, the errors could not be projected, but could only be used as an indication of a problem within DoD. The Military Department auditors made recommendations to the organizations involved in this review. The errors identified did not represent a systemic DoD-wide problem. Accordingly, we made no additional recommendations.

Testing the Key Data Elements for Accuracy

The second implementation strategy addressed the issue of valuing general property, plant, and equipment in the Military Departments. Specifically, if the databases did not contain cost data or did not have supporting documentation for the cost data entered on the property records, DoD would need to develop an appropriate methodology to estimate the Government cost to acquire, construct, or improve real property. Accordingly, the Military Department auditors determined whether data in the following key data element fields were accurate: category code and description, unit of measure (for example, square footage), dates, ownership, and condition code. The data contained in those key fields are critical to the application of alternative methods for estimating historical cost. In addition, the auditors determined whether the real property assets had supporting documentation for assigned cost values.

To validate those key data elements and assigned cost values, the auditors reviewed source documentation, independent of the automated databases. For example, to validate the unit of measurement, the auditors used the latest DD Form 1354, asset diagrams, blueprints, or other engineering documentation. For the condition code, the auditors assessed the physical condition of the asset to the definition of the condition code. For assigned cost values, the auditors used the DD Form 1354 or its equivalent. The Military Department real property officials were not aware of the types of documentation that should be retained to document the key data elements and assigned cost values. The real property officials either provided the DoD audit community with inconsistent source documentation or provided no documentation at all. The real property officials used various source documents or did not retain documents because

DoD did not provide the Military Departments with specific guidance on the acceptable source documents that they should retain to validate the key data elements and assigned cost values.

The lack of source documentation to support the cost to acquire, construct, or improve real property required the contractor to estimate the historical cost. However, to accurately calculate the historical cost estimate, the contractor needed source documentation to support the key data elements. With the year built, unit of measure, and category code, the contractor could use various appraisal methodologies to estimate the historical cost of real properties. Without that information, estimating historical cost would be either impractical or extremely difficult.

The test results of the key data elements and assigned cost values in the real property databases were inconclusive because DoD policy guidelines did not specify or define the specific documentation for the Military Departments to maintain to support key data elements and assigned cost values. As a result, the key data elements needed to estimate the historical cost could not be used to validate the \$71.2 billion of real property reported on the DoD Agency-Wide financial statements for FY 1998.

Summary

Statistical sampling testing for existence showed that real property databases at the Military Departments contained reasonably accurate inventories of real property reported at individual values of greater than \$100,000. But the portion of the Air Force real property database with individual reported values of less than \$100,000 was not so accurate. The Army had one or more completeness errors at half of the locations tested partially because of a system conversion problem. The test of the accuracy of key data elements and assigned cost values in the real property databases was inconclusive because documentation to support the accuracy of the key data elements and assigned cost values was inconsistent.

DoD guidance should specify the source documentation that Military Departments should retain to validate the key data elements and assigned cost values. Although real property databases were generally accurate for existence, the errors identified may impact the Under Secretary of Defense (Comptroller) effort to value the real property.

Recommendation, Management Comments, and Audit Response

We recommend that the Under Secretary of Defense (Comptroller) issue interim policy that specifies the supporting documentation that the Military Departments should retain to validate Government cost to acquire, construct, or improve real property. The Under Secretary should then incorporate the guidance in the Department of Defense Financial Management Regulation in its update.

Under Secretary of Defense (Comptroller) Comments. The Deputy Chief Financial Officer stated that his office is in the process of revising the “Department of Defense Financial Management Regulation” to specify the supporting documentation that should be retained to validate the cost to acquire, construct, or improve real property. In addition, the Deputy Chief Financial Officer stated that the Inspector General, DoD, should have known that the guidance was in process, making the recommendation unnecessary.

The Deputy Chief Financial Officer also stated that the draft report implies that the Department’s effort to value real property may be adversely impacted by key data element errors. According to the Deputy Chief Financial Officer, the draft report neither identified specific problems with the key data elements nor presented appropriate recommendations to remedy the problems. The Deputy Chief Financial Officer considered our references to the problem as vague, not helpful, and a disservice to the Department.

The Deputy Chief Financial Officer strongly believes that our conclusion is irrelevant on the reliability of real property databases in the Air Force if the capitalization threshold is lowered. The potential outcome of the ongoing study of the capitalization threshold would not support our conclusions. According to the Deputy Chief Financial Officer, our comments were gratuitous and not informative or constructive.

Lastly, the Deputy Chief Financial Officer noted a definition error for existence and completeness in the Background of the draft report.

Audit Response. The Deputy Chief Financial Officer’s comments were nonresponsive. The Deputy Chief Financial Officer provided no planned date for reissuing the guidance and no draft guidance has been provided to this office for comment. Past experience indicates that revising guidance is a lengthy process and we believe that the Department’s best interest would be served by accelerating matters. We have revised the recommendation to provide that the Under Secretary issue interim guidance stating the requirements. When the Deputy Chief Financial Officer next updates the Department of Defense Financial Management Regulation, it should incorporate the new policy.

The auditors’ review of the key data elements, although not statistically demonstrable, did provide insight into the problems with documentation. The auditors found that real property officials did not know about the necessity to keep the documents that provide independent proof of the elements for cost, year built, and measurement of the property. An appraiser needs all of those key data elements to calculate a value for most property. The errors were brought to the Department’s attention to assist with the implementation strategy that requires DoD to value real property with the help of a contractor. If the real property officials and the contractors cannot find source documentation to support the key data elements, then the appraisers must find alternative means of obtaining the data, which may prove more costly.

The Deputy Chief Financial Officer’s comments on the reliability of the Air Force database if the threshold is lowered did not address the major issue. If the capitalization threshold were lowered, the Air Force database may not reliably reflect items for existence. Reliability is a concern because the real property officials did not appear to provide the same level of attention to assets with a reported value of less than \$100,000 as to assets with a reported value of

greater than \$100,000. Real property officials may not have included items with a reported value of less than \$100,000 in the real property databases. The cost of an asset, be it a \$100,000, \$90,000, or \$1,000, should not affect the accountability required and, accordingly, our conclusions were relevant. Our report provided information that real property officials need to improve visibility over all assets, regardless of value. The Air Force Audit Agency believed that the problems were significant; consequently, they made base level recommendations. Those recommendations were constructive and will help Air Force real property management.

We appreciate the Deputy Chief Financial Officer pointing out the reversed definitions for existence and completeness in the Background section of the draft report, which we revised. The definitions were stated correctly throughout the remainder of the report.

We request that the Under Secretary of Defense (Comptroller) provide comments on the revised recommendation.

Army Comments. Although not required to comment, the Department of the Army Assistant Chief of Staff for Installation Management agreed with the report. In addition, the comments noted that the Army issued policy instructing the installation real property accountable officers to maintain records of capitalization and capital improvements of real property for the lifetime of all facilities.

Audit Response. We commend the Army for the action taken and the positive tone of its comments.

Appendix A. Audit Process

Scope and Methodology

Work Performed. In this financial-related audit, the Military Department audit agencies assessed the reliability of the real property databases in the Military Departments to include the Asset Cost Table in CEFMS in the Corps of Engineers. The AAA used the real property databases from the Headquarters Executive Information System as of March 31, 1998, and the Asset Cost Table from CEFMS as of August 20, 1998. The NAS and the Air Force Audit Agency used the September 30, 1997, real property databases in the Navy Facility Assets Data Base and the Interim Work Information Management Systems, respectively. The Service auditors performed their audit work, with assistance from the General Accounting Office and the Inspector General, DoD, at the real property offices at the military installations and interviewed real property officials to verify the existence and completeness of the databases. The auditors also reviewed the real property records that were contained in the databases. As of September 30, 1998, the real property value reported on the financial statements for both general and working capital funds was \$68.7 billion. The Army reported \$11.7 billion, the Corps of Engineers reported \$25.5 billion, the Navy reported \$16.7 billion, and the Air Force reported \$14.8 billion. The other Defense agencies reported \$2.5 billion, for a total of \$71.2 billion in real property. Real property included land, facilities, structures, and leasehold improvements.

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

- **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 in the following area objectives and goals.

- **Objective:** Consolidate finance and accounting operations.
Goals: Consolidate finance and accounting center operations.
(FM-1.1) Consolidate finance and accounting field operations.
(FM-1.2) Consolidate and standardize financial systems. **(FM-2.1)**
Reduce and improve accounting systems. **(FM-2.2)**

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- **Objective:** Reengineer DoD business practices. **Goals:** Standardize, reduce, clarify, and reissue financial management policies. (FM-4.1) Improve data standardization of finance and accounting data items. (FM-4.4)
 - **Objective:** Strengthen internal controls. **Goal:** Improve compliance with Federal Managers Financial Integrity Act. (FM-5.3)
 - **Objective:** Become a mission partner. **Goal:** Facilitate process improvement. (ITM-1.3)
 - **Objective:** Provide services that satisfy customer information needs. **Goals:** Modernize and integrate Defense information infrastructure. (ITM-2.2) Upgrade technology base. (ITM-2.3)

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

Use of Computer-Processed Data. To achieve the audit objectives, the Military Department auditors relied extensively on computer-processed data contained in several systems. The AAA relied on the Headquarters Executive Information System and the Integrated Facilities System in the Army and the CEFMS in the Corps of Engineers. The NAS used the Navy Facility Assets Data Base in the Navy, and the Air Force Audit Agency used the Interim Work Information Management System in the Air Force.

Although system controls were not reviewed, the Military Department auditors; the General Accounting Office; and the Inspector General, DoD, could rely on the data from the systems. They assessed the reliability of the data by physical observation and examination of the property items sampled from the databases. The information provided by the computer-processed data was compared with the actual real property item. The observed and examined real property items were not significantly different from the computer-processed data; consequently, we could rely on the computer-processed data.

Statistical Sampling Methodology. Each Military Department audit agency developed its own sampling methodology and plan. However, the Inspector General, DoD, reviewed and approved each plan as well as the results of the sample. To begin tests of existence, each audit organization drew a statistical sample, approved by the Inspector General, DoD, from their real property databases and verified the existence of each sample item. To pass the existence testing, the 90 percent upper bound of the estimated error rate had to be less than 5 percent. To test completeness, the auditors judgmentally selected 10 items, if available, at each location where existence testing was performed and traced the selected items back to the real property database to verify that they were included. If an item was not recorded in the real property database, the auditors interviewed real property officials to determine ownership of the asset. If the asset was "owned" or there was an "interest" in the asset (for example, the capital lease arrangement) by the military component being tested but the asset was not recorded in the real property database, the auditor recorded a completeness error.

Use of Technical Assistance. We obtained the assistance of statistical advisors from the three Military Department audit agencies and from the Inspector General, DoD. The Service statistical advisors developed the sampling methodologies and plans. At the end of the audit, the Service statistical advisors developed the sampling results and conclusions as to the reliability of the databases for existence. The Inspector General, DoD, statistical advisor reviewed and approved the plans and reviewed and approved the statistical results.

Audit Type, Dates, and Standards. We performed this financial-related audit from July 1998 through April 1999 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. Our scope was limited in that we did not include full tests of internal or management controls. Those controls will be tested in a related audit on additions and deletions of real property.

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

Appendix B. Summary of Prior Coverage

Inspector General, DoD

Inspector General, DoD, Report No. 98-097, "Defense Commissary Agency Financial Reporting of Property, Plant, and Equipment," March 27, 1998.

Inspector General, DoD, Report No. 98-135, "Implementation of the Defense Property Accountability System," May 18, 1998.

Inspector General, DoD, Report No. 98-008, "Financial Reporting of Defense Business Operations Fund FY 1996 Property, Plant, and Equipment," October 9, 1997.

Inspector General, DoD, Report No. 97-148, "Defense Logistics Agency Actions to Improve Property, Plant, and Equipment Financial Reporting," May 29, 1997.

Inspector General, DoD, Report No. 96-212, "Capitalization of the Department of Defense General Property, Plant, and Equipment," August 19, 1996.

Inspector General, DoD, Report No. 95-034, "Development of Property, Plant, and Equipment Systems Within the Department of Defense," November 21, 1994.

Inspector General, DoD, Report No. 94-149, "Property, Plant, and Equipment Accounts on the Financial Statements of the Defense Logistics Agency Business Areas of the Defense Business Operations Fund for FY 1993," June 28, 1994.

Army

Army Audit Agency Report No. AA97-149, "Army's Principal Financial Statements for Fiscal Years 1996 and 1995, Financial Reporting of Real Property, Natural Resources, and Leases," September 30, 1997.

Army Audit Agency Report No. WR 95-201, "Building Accountability and Use," November 18, 1994.

Navy

Naval Audit Service Report No. 051-97, "Department of the Navy Fiscal Year 1996 Annual Financial Report: Property, Plant, and Equipment, Net," September 25, 1997.

Air Force

Air Force Audit Agency Project No. 96068011, "Air Force Defense Business Operations Fund Cash Management and Property, Plant, and Equipment, Fiscal Year 1996," July 30, 1997.

Air Force Audit Agency Project No. 95053002, "Property, Plant, and Equipment, Fiscal Year 1995 Air Force Consolidated Financial Statements," June 13, 1996.

Air Force Audit Agency Project No. 94053032, "Review of Property, Plant, and Equipment, Fiscal Year 1994 Air Force Consolidated Financial Statements," August 10, 1995.

Air Force Audit Agency Project No. 94068021, "Financial Reporting of Fiscal Year 1993 Property, Plant, and Equipment Within the Transportation Services Business Area," July 11, 1994.

Air Force Audit Agency Project No. 93068010, "Financial Reporting of Fiscal Year 1993 Property, Plant, and Equipment Within the Depot Maintenance Service and Supply Management Business Areas," July 1, 1994.

Appendix C. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Comptroller)
Deputy Chief Financial Officer
Deputy Comptroller (Program/Budget)
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 Commissary Agency
Director, Defense Contract Audit Agency
Director, Defense Finance and Accounting Service
Director, Defense Finance and Accounting Service Columbus Center
Director, Defense Finance and Accounting Service Indianapolis Center
Director, Defense Logistics Agency
Director, National Security Agency
Inspector General, National Security Agency
Inspector General, Defense Intelligence Agency
Director, Defense Systems Management College

Non-Defense Federal Organizations and Individuals

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

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

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 Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Reform
House Subcommittee on Government Management, Information, and Technology,
Committee on Government Reform
House Subcommittee on National Security, Veterans Affairs, and International
Relations, Committee on Government Reform
House Subcommittee on Technology, Committee on Science

Under Secretary of Defense (Comptroller) Comments

Final Report
Reference



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

JUL 20 1999

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

SUBJECT: Department of Defense Inspector General Draft Audit Report, "Reliability of the
Military Departments' Real Property Databases for Existence and Completeness"
(Project No 9FH-3001 00)

This memorandum is in response to your request for comments on the subject draft audit report. The report recommends that the Under Secretary of Defense (Comptroller) issue policy specifying the supporting documentation that the Military Departments should retain to validate the cost to acquire, construct, or improve real property

As the OIG knows, this office is in the process of revising the "Department of Defense Financial Management Regulation" ("DoDFMR") to specify the supporting documentation that should be retained to validate the cost to acquire, construct, or improve real property. A recommendation for this office to do exactly what it is in the process of doing, with no further recommendations for additional action, reaffirms that this office is doing what needs to be done. However, since the OIG was aware that this office already was taking such action, it is unclear why a formal audit recommendation was made. Given the administrative burden placed on both the OIG and this office by a formal audit recommendation, it would seem that both offices would be better served if the Department's ongoing actions simply had been noted in the report. A formal recommendation to do what already is being done would appear to be of little benefit to either office.

The draft report infers that the Department's efforts to value real property may be adversely impacted by key data element errors. This inference is particularly troubling in light of the fact that the Department is investing millions of dollars to value its real property. If the OIG believes that the expenditure of these funds by the Department is at risk and that the Department may not achieve the desired results, then the Department would benefit from the identification and presentation of specific problems along with appropriate recommendations. Vague references to potential difficulties are not helpful and are a disservice to the Department.

The draft report also states that the reliability of the Air Force property databases would be impacted adversely if the capitalization threshold were lowered. This conclusion is irrelevant to the current threshold and not placed in the proper context for consideration, by the reader, of potential changes. As the OIG is aware, the Department is reviewing its current capitalization threshold policy. However, that fact is not addressed in the draft report. As a result of the ongoing review, one of five primary potential outcomes is possible. The capitalization threshold

Revised

Emphasis
added

Final Report
Reference

could: (1) remain at its current level; (2) be lowered, with retroactive implementation; (3) be lowered, with prospective implementation; (4) be raised, with retroactive implementation; or (5) be raised, with prospective implementation. These potential outcomes also are not addressed. The Air Force property database could be adversely impacted only if the second potential outcome listed above were to occur (the most unlikely of the five potential outcomes) and the Air Force took no further action to improve the reliability of its database (also a very unlikely scenario). A failure to place the comments on the Air Force's database in the proper context and to address the likely impact for each of the Military Departments under each of the five potential outcomes makes the applicable comments appear to be gratuitous and not informative or constructive.

Revised

Lastly, the draft report is factually incorrect. On page one of the report, the definitions for existence and completeness are reversed. Existence pertains to whether an asset recorded in the database actually exists, and completeness pertains to whether assets observed are actually recorded in the database

This office appreciates the opportunity to comment on the draft report. The point of contact for this matter is Mr. Michael Powers. Mr. Powers may be reached by e-mail: powersm@osd.pentagon.mil or by telephone at (703) 697-0536.



Nelson Toye
Deputy Chief Financial Officer

Department of the Army Comments



REPLY TO
ATTENTION OF

DEPARTMENT OF THE ARMY
ASSISTANT CHIEF OF STAFF FOR INSTALLATION MANAGEMENT
600 ARMY PENTAGON
WASHINGTON DC 20310-0800



JUL 06 1999

DAIM-MD (405-45)

7/6/99
ARUEL J. EDENS, JR., LTC, GS, DDECC
MEMORANDUM THRU THE DIRECTOR OF THE ARMY STAFF

Paul W. Johnson
Deputy Assistant Secretary of the Army,
(Installations and Housing)
CASA (I, L&E)

~~ASSISTANT SECRETARY FOR THE ARMY (INSTALLATIONS
AND ENVIRONMENT)~~

8 JUL 1999

FOR THE OFFICE OF THE INSPECTOR GENERAL, DEPARTMENT OF DEFENSE (DoD)
(DIRECTOR OF FINANCE AND ACCOUNTING)

SUBJECT: Reliability of the Military Departments Real Property Databases for Existence and
Completeness (Project No. 9FH-3001.00)

1. Reference: IG, DOD memorandum dated 4 June 1999, with draft report.
2. The Assistant Chief of Staff for Installation Management has reviewed the subject report and concurs with report as written
3. Under your summary of recommendations, you state the Under Secretary of Defense (Comptroller) should issue policy specifying the supporting documentation that the Military Departments should retain to validate the cost to acquire, construct, or improve real property. Please note the Army issued policy on 10 Aug 98, instructing the installation real property accountable officers to maintain records pertaining to capitalization and capital improvements of real property for the lifetime of all facilities.
4. For further information contact Ms. Julie Jones at commercial (703) 692-9223, DSN 222-9223, or email jonesil@hqda.army.mil.

R.L. Van Antwerp

R.L. Van Antwerp
Major General, U.S. Army
Assistant Chief of Staff
for Installation Management

CF:
ASA(FM&C)
SAAG-PMO-S
SALL-IL
SAPA-ZX

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The Finance and Accounting Directorate, Office of the Assistant Inspector General for Auditing, DoD, prepared this report.

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