

Inspector General

United States
Department of Defense



Internal Controls Over Government Property in the Possession of Contractors at Two Army Locations

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Acronyms and Abbreviations

AAA	Army Audit Agency
AFARS	Army Federal Acquisition Regulation Supplement
AMC	Army Materiel Command
AR	Army Regulation
DPAS	Defense Property Accountability System
FAR	Federal Acquisition Regulation
FMR	Financial Management Regulation
GFP	Government-Furnished Property
IG	Inspector General
PBO	Property Book Officer
RFAAP	Radford Army Ammunition Plant



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

June 18, 2009

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR ACQUISITION,
TECHNOLOGY, AND LOGISTICS
UNDER SECRETARY OF DEFENSE (COMPTROLLER)/
DOD CHIEF FINANCIAL OFFICER
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING
SERVICE
AUDITOR GENERAL, DEPARTMENT OF THE ARMY

SUBJECT: Internal Controls Over Government Property in the Possession of
Contractors at Two Army Locations (Report No. D-2009-089)

We are providing this report for review and comment. The Army Installation Management Command did not respond to the draft report; however, we considered comments from the Army Materiel Command when preparing the final report.

DoD Directive 7650.3 requires that all issues be resolved promptly. Comments from the Army Materiel Command were partially responsive. As a result of those comments, we revised Recommendation 1.a. to clarify our intention. We request that the Army Materiel Command provide comments on Recommendation 1.a., and the Army Installation Management Command provide comments on all recommendations by July 20, 2009.

If possible, please send management comments in electronic format (Adobe Acrobat file only) to AUDDBO@dodig.mil. Copies of the management comments must contain the actual signature of the authorizing official. We cannot accept the / Signed / symbol in place of the actual signature. If you arrange to send classified comments electronically, they must be sent over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 601-5868 (DSN 329-5868). If you desire, we will provide a formal briefing on the results.

Patricia A. Marsh
Patricia A. Marsh, CPA
Assistant Inspector General
Defense Business Operations



Results in Brief: Internal Controls Over Government Property in the Possession of Contractors at Two Army Locations

What We Did

Our objective was to evaluate the Department of the Army internal controls over Government-furnished property. Specifically, we examined databases and processes at the Radford Army Ammunition Plant (RFAAP) in Virginia and at Fort Irwin, California, that accounted for existence, completeness, and valuation of Government property in the possession of contractors.

What We Found

The Army did not have adequate internal controls for the existence, completeness, and valuation of Government property in the possession of contractors at RFAAP and Fort Irwin. Specifically, the internal controls were not effective for financial reporting and accountability of Government property, valued at \$169.6 million. For example, personnel at RFAAP and Fort Irwin did not:

- report 5 of 45 samples, depreciate 16 of 45 samples, or adequately support capital assets for 36 of 45 samples;
- properly document the transfer of property accountability to contractors; or
- provide adequate contract oversight for record-keeping, physical inventory, and identification of Government property.

Material internal control weaknesses resulted from noncompliance with DoD and Army guidance for financial reporting, contract administration, and property accountability and insufficient oversight processes for Government property. As a result, the Army financial statements and databases were misstated. In addition, the two Army locations may not be able to safeguard Government property from

unauthorized use, destruction, or loss. Implementing the recommendations should resolve these weaknesses.

What We Recommend

To resolve the control weaknesses over Government property in the possession of contractors, the Army should:

- require contractors to provide updates to capital assets in their property system to Property Book Officers or Property Administrators;
- require installations to certify the accuracy and completeness of data entered into the financial reporting system;
- redefine functional roles and responsibilities; and
- enforce and monitor compliance with established guidance.

Management Comments and Our Response

The Army Installation Management Command did not provide comments. The Army Materiel Command (AMC) agreed with all but one recommendation, and its comments were mostly responsive. Specifically, AMC disagreed with requiring contractors to use and update the Defense Property Accountability System because Federal guidance allows contractors to use their system.

We agree; however, contractors also were not providing updates on capital assets; therefore, we revised our recommendation. We request that AMC provide further comments and that the Army Installation Management Command comment by July 20, 2009. Please see the recommendations table on the back of this page.

Recommendations Table

Management	Recommendations Requiring Comment	No Additional Comments Required
Commanding General, Army Materiel Command	1.a.	1.b., 1.c., 1.d., 1.e., 2.a., 2.b., and 3.
Commanding General, Army Installation Management Command	1.a., 1.b., 1.c., 1.d., 1.e., 2.a., 2.b., and 3.	

Please provide comments by July 20, 2009.

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Introduction

Objectives

Our overall objective was to evaluate the Department of the Army internal controls over Government-furnished property. Specifically, we examined whether the processes and databases at the RFAAP, located in Virginia, and at Fort Irwin, located in California, accurately accounted for existence, completeness, and valuation of Government property transferred from and retained by contractors. We examined whether the Army clearly defined its requirements for the accountability and reporting of Government-furnished property. See Appendix A for a discussion of scope and methodology. Appendix B provides a glossary of technical terms used in this report.

Background

According to Public Law 101-576, Chief Financial Officers Act of 1990, as amended, agency Chief Financial Officers must develop and maintain an integrated agency accounting and financial management system, including financial reporting and internal controls. The Chief Financial Officers Act requires that financial reporting and internal controls comply with applicable accounting principles, standards, and requirements, as well as internal control standards. In addition, the financial reporting and internal controls must provide complete, reliable, and timely information that is consistently prepared and that is responsive to the financial information needs of agency management. This report discusses the adequacy of internal controls used to account for Government property in the possession of contractors. Accurate reporting of Government property in the possession of contractors is essential for an agency to comply with the Chief Financial Officers Act of 1990.

Federal Acquisition Regulation

In the September 19, 2005, Federal Register, the Civilian Agency Acquisition Council and the Defense Acquisition Regulation Council proposed to amend the Federal Acquisition Regulation (FAR) to simplify procedures, clarify language, and eliminate obsolete requirements related to the management and disposition of Government property in the possession of contractors. In June 2007, the revised Part 45 of the FAR was published.

FAR Part 45, "Government Property," June 2007, defines Government-furnished property (GFP) as property in the possession of, or directly acquired by, the Government and subsequently made available to a contractor. Examples of GFP include facilities, materials, special tooling, special test equipment, and agency-peculiar property. The FAR further defines Government property as all property owned or leased by the Government.

GFP is included in the General Property, Plant, and Equipment line of the Balance Sheet. DoD Components are required to record detailed information on property provided to

contractors, including real property (such as Government-owned, contractor-operated facilities) and DoD property transferred from one contract to another contract in DoD property accountability systems. DoD property procured or fabricated by a contractor is required to be accounted for and reported by the contractor until the property is recorded in DoD property accountability records or systems. Contractors are responsible and liable for Government property in their possession, unless otherwise provided for in the contract.

Radford Army Ammunition Plant

RFAAP, located in Radford, Virginia, is a Government-owned, contractor-operated facility. A Government-owned, contractor-operated partnership allows each partner to perform duties for which it is uniquely suited. For example, the Government establishes mission areas, and the private sector implements the missions, using best practices. The RFAAP mission is to provide U.S. warfighters with propellants and munitions. In January 1995, the Army entered into a facilities contract for the use, maintenance, accountability, and disposition of GFP at RFAAP. In April 2003, the Government property was transferred from the facilities-use contract to the current facilities contract. Total plant workforce as of September 30, 2006, consisted of approximately 1,350 contractors, 28 Government civilians, and 1 military member.

Fort Irwin

The Installation Management Command at Fort Irwin, California, provides the Army the installation capabilities and services to support expeditionary operations in a time of persistent conflict, and provides a quality of life for soldiers and families commensurate with their service. In September 2000, the Army entered into the current contract to perform installation support services, such as facilities maintenance, law enforcement, and fire and emergency response services at Fort Irwin.

Review of Internal Controls

We determined that material internal control weaknesses in the Department of the Army existed at RFAAP and Fort Irwin, as defined by DoD Instruction 5010.40, "Managers' Internal Control Program Procedures," January 4, 2006. The Army internal controls over its processes and databases did not accurately account for the existence, completeness, and valuation of Government property in the possession of contractors. Implementing our recommendations will improve property accountability and financial reporting of Government property. We will provide a copy of this report to the senior Army official responsible for internal controls in the Department of the Army.

Internal Controls Over Government Property in the Possession of Contractors at Two Army Locations

Army internal controls over its processes and databases did not accurately account for the existence, completeness, and valuation of Government property in the possession of contractors at RFAAP, Virginia and Fort Irwin, California. Specifically, the Army internal controls at these locations did not ensure that personnel:

- reported 5 of 45 samples, depreciated 16 of 45 samples, or adequately supported capital assets for 36 of 45 samples;
- maintained accurate accountable property records for 3 of 59 samples costing a total of \$542,014, and for 4 of 49 samples costing \$5,000 or more;
- performed required inventory counts for 6,328 of 34,152 assets;
- identified and segregated Government property for 6 of 109 samples; or
- properly transferred or updated accountability records.

Controls were not effective because Army personnel did not follow the DoD and Army guidance for financial reporting, contract administration, and property accountability of Government property in the possession of contractors. Additionally, the Army did not have processes to provide adequate contract oversight for Government property at these two locations.

As a result, Army financial statements and databases were misstated for the two locations we reviewed. In addition, RFAAP and Fort Irwin may not be able to: produce reliable information for decision-making; safeguard Government property from unauthorized use, destruction, or loss; and track and use assets for support of Army operations.

Army Property Systems

On December 22, 1994, the Office of the Secretary of Defense designated the Defense Property Accountability System (DPAS) as the property accountability system to be used to provide DoD property and financial information, which is reported to the Defense Finance and Accounting Service. Specifically, DPAS provides the capability to account for Government-furnished property, compute depreciation, and report disposals. RFAAP and Fort Irwin used DPAS to report financial information and account for Government property in the possession of contractors.

The contractors accounted for Government property in their care using their own property management systems, instead of DPAS. The RFAAP contractor used a Microsoft Access

database to account for Government property. The Fort Irwin contractor accounted for the Government property in a Costpoint Property Management system and two Microsoft Word documents. Neither contractor system was able to interface with DPAS to transfer data.

RFAAP provided a universe of 34,152 assets recorded in its Access database as of September 13, 2007. Fort Irwin provided a universe of 16,928 assets as of November 5, 2007, of which 16,574 assets were from the Costpoint system and 354 assets were from the Microsoft Word documents. From those universes, we selected samples to test the existence, completeness, and valuation of Government property in the possession of contractors (see Table 1).

Table 1. Government Property Tested

	RFAAP		Fort Irwin		Total	
	No. of Assets	Value (millions)	No. of Assets	Value (millions)	No. of Assets	Value (millions)
Universe	34,152	\$132.38	16,928	\$37.20	51,080	\$169.58
Valuation	31	\$9.28	14*	\$2.52	45	\$11.80
Existence	44	\$2.84	15	\$.01	59**	\$2.85
Completeness	35	\$1.07	15	\$.02	50**	\$1.09

*We selected 15 assets but tested 14 because the contractor at Fort Irwin erroneously recorded one sample as \$374,085 in the contractor’s property management system; however, documentation showed the item’s value as \$374.85.

**We tested 109 assets in the contractor’s property management system, which included 59 assets tested for existence and 50 assets tested for completeness.

Financial Data and Processes

Reliable financial information is critical to reducing Government waste, balancing the budget, and increasing management’s performance capabilities. The Army should have ensured that its financial statements consistently reported and depreciated assets in the possession of contractors and that they adequately supported the recorded values of its assets.

Reporting Capital Assets

RFAAP and Fort Irwin did not consistently report capital assets as required by DoD Financial Management Regulation (FMR) and Army regulations. The DoD FMR, volume 4, chapter 6, “Property, Plant, and Equipment,” July 2006, requires the Army to report capital assets in the financial statements, even if they are in the possession of contractors. In addition, in Army Regulation (AR) 710-2, “Inventory Management Supply Policy Below the National Level,” July 8, 2005, the DoD Deputy Secretary of Defense mandated DPAS as the system of record for General Property, Plant, and Equipment costing more than \$100,000 for Chief Financial Officers Act purposes. However, the Army did not capture 5 of 45 capital assets, Fort Irwin 2 and RFAAP 3, valued at \$1.8 million, in DPAS.

For example, RFAAP had not entered additions or deletions of capital assets into DPAS since FY 2005. According to RFAAP personnel, the Army hired a contractor to enter financial information for all assets with an acquisition value greater than \$5,000 into DPAS. Additionally, in FY 2005, the Comptroller of the Army provided about \$64,000 to support Government-owned, contractor-operated facilities converting to DPAS. However, the Comptroller of the Army has not provided funds for maintenance of DPAS since the conversion. Consequently, RFAAP has neither maintained DPAS nor modified its contract for the contractor to update DPAS since FY 2005. Assistant Secretary of the Army (Financial Management and Comptroller) personnel, who compiled data from DPAS for the Army financial statements, were not aware that RFAAP was not updating DPAS until we brought it to their attention in January 2008.

In another instance, Fort Irwin did not report two capital assets valued at \$757,373. The Installation Property Book Officer (PBO) stated that some capital assets may not be recorded if the Property Administrator does not provide information for him to enter the property data into DPAS, as required by the Installation Standard Operating Procedures. The procedures require the contracting office's designated representative to notify the PBO when the contractor receives, transfers, or disposes of any GFP. Some capital assets were not recorded because the PBO was not notified. Requiring RFAAP and Fort Irwin to certify, each year, that property financial data were accurate and complete would improve the consistency of the capital assets reported in the Army financial statements.

Depreciation

Of 45 sampled assets, RFAAP and Fort Irwin did not depreciate 16 assets valued at \$3.4 million in accordance with the DoD FMR. For example, Fort Irwin did not depreciate 13 of 14 assets. However, the DoD FMR, volume 4, chapter 6, requires all property that equals or exceeds the capitalization threshold of \$100,000 to be depreciated. To capture depreciation in DPAS, personnel at Fort Irwin had to activate the depreciation function when entering information. However, the installation PBO responsible for entering the assets did not activate the function. He stated that the Property Book Office was not assigned this duty, and he thought that the function should be the responsibility of the financial division. As a result, the Army financial statements did not accurately report the value of Government property in the possession of contractors. The Army could improve the accuracy of the financial data by assigning the PBO financial reporting responsibility.

Supporting Documentation

For 36 of the 45 assets, valued at \$8.1 million, RFAAP and Fort Irwin did not maintain supporting documentation as required by the DoD FMR and Army regulations. The DoD FMR, volume 4, chapter 6, provides a list of supporting documents that may be used to support the property acquisitions. The list includes invoices, signed acceptance documents, and material inspection and receiving reports. In addition, AR 710-2 requires that all source documentation supporting the initial purchase of capital equipment greater than or equal to \$100,000 be maintained on a permanent basis. However, neither RFAAP nor Fort Irwin could provide the required documentation to support the recorded value of capital equipment.

For example, Holston Army Ammunition Plant transferred a locomotive, valued at \$185,000, to RFAAP using DA Form 2408-9, “Equipment Control Record.” The DoD FMR recognizes DA Form 2408-9 as valid supporting documentation. However, RFAAP received a DA Form 2408-9 that was incomplete because it did not contain the cost information of the locomotive. Contractor personnel stated that the receiving contractor phoned the Holston Army Ammunition Plant to obtain the value of the locomotive and, without obtaining any reliable documentation, the receiving contractor typed the cost information on the DA 2408-9. Without documentation to support the stated cost information, the recorded value of the locomotive is not considered reliable.

At Fort Irwin, Army personnel recorded a water truck in DPAS for \$6,211, but the contractor’s property management system recorded the water truck for \$112,748. The installation PBO stated that when documentation is not available to support the data entered into DPAS, the PBO populates the missing information from the Federal Logistics Data catalog using the line-item number. Because the Federal Logistics Data was used to populate missing information instead of valid supporting documentation, it caused a discrepancy between the two systems for 5 of 14 sampled items, as shown in Table 2. Without adequate supporting documentation, we could not validate the cost and purchase dates recorded in DPAS. Consequently, RFAAP and Fort Irwin financial information could be materially misstated.

Table 2. Comparison of Cost Records in Absolute Values

Property No.	Cost in Contractor System	Costs in DPAS	Discrepancy
D04763	\$160,466	\$172,171	\$11,705
D06046	128,259	110,751	17,508
D07675	105,329	217,297	111,968
D06412	205,785	454,500	248,715
D10002	112,748	6,211	106,537

Accountability Data and Processes

Accountability is critical to maintaining timely and accurate information on the status and identity when property moves from contract to contract. Because contractors are responsible for Government property in their possession, the Army should have ensured that the contractors had effective internal controls in place to manage and account for Government property in their possession. In addition, the Army should have maintained accurate asset information by recording GFP with a unit cost of greater than \$5,000 in the Army property accountability system, DPAS.

Existence

DoD Instruction 5000.64, “Accountability and Management of DoD-Owned Equipment and Other Accountable Property,” November 2006, states that accountable property records must reflect the current status and location of property until disposition. RFAAP contracts require that contractors maintain records for the official Government property

in their care. However, of the 59 assets that were recorded in the RFAAP contractor's property management system, 3 of them, valued at a total of \$542,014, could not be located. For example, the contractor did not remove the records of a demolished building from its property management system. As a result, the contractor's property management system did not accurately reflect property in the contractor's possession.

Completeness of Database

The AR 710-2 requires that Government-furnished equipment costing more than \$5,000 be accounted for in the Army property book system. Of 109¹ samples we tested for existence and completeness in the contractor's property management system, 49 cost \$5,000 or more. The other 60 samples were less than \$5,000 in value and were therefore not required to be input into DPAS. However, we included the 60 samples in the existence and the completeness reviews because they were in the possession of contractors. RFAAP did not maintain records for 4 of the 49 assets in DPAS, as required by AR 710-2. Property records showed that the four assets, valued at \$473,342, were acquired by RFAAP after an Army contractor updated DPAS in 2005. As a result, DPAS did not accurately account for assets costing \$5,000 or more.

Physical Inventories

The FAR 45.508, "Physical Inventories," August 2005, requires that contractors periodically perform a physical inventory of all Government property in their possession or control, as well as immediately upon termination or completion of a contract. However, RFAAP did not perform a complete inventory at the end of a contract in FY 2003. The RFAAP contractor property accountability database showed that 6,328 of 34,152 assets were not included in the close-of-contract physical inventory.

The contractor stated that the FAR Class Deviation 99-00008, July 13, 1999, waived the inventory requirement. The class deviation, cancelled on July 30, 2007, reduced the level of record-keeping and physical inventory requirements for low-value property (costing less than \$5,000). Additionally, it allowed the contractors to defer reporting loss, damage, or destruction of assets until contract termination or completion. However, the class deviation required, at a minimum, an inventory count for low-value property at the close of the contract.

RFAAP personnel did not clarify the inventory requirements and concurred with the contractor on the waiver. As a result, the physical inventory count records did not accurately reflect actual inventory of Government property in the possession of contractors and may also increase the risk of unauthorized use, destruction, or loss of property.

¹ For the completeness and existence testing, we tested 109 samples from the contractor's property management system. However, for the completeness of database section of the report we selected 49 of these assets costing \$5,000 or more to be tested in the Army's database, DPAS.

Property Tag and Ownership

For 6 of 109 sampled assets, RFAAP did not ensure that the contractors either placed an identification tag on the Government property or maintained physical segregation of Government property in accordance with DoD Manual 4161.2-M, “DoD Manual for the Performance of Contract Property Administration,” December 1991. The DoD manual states that a contractor must identify and mark Government property during the contractor’s receiving process. It further states that proper identification serves to ensure that the Government’s assets are not confused with contractor-owned property and are not used for unauthorized purposes. However, at RFAAP, one asset sold to a contractor still had its Government identification tag. In addition, we noted items without identification tags that were commingled with Government property. Contractor personnel stated that those assets were either contractor-owned or valued at less than \$200. However, without proper identification or physical segregation, there is potential for the unauthorized use of Government property.

System Review

According to FAR 45.104, “Review and Correction of Contractors’ Property Control System,” August 2005, contract administration responsibilities must include the review and approval of the contractor’s property control systems. In addition, DoD Manual 4161.2-M requires organizations to perform at least one system analysis each fiscal year. Fort Irwin management created a plan to conduct the system analysis. However, management did not approve and implement the plan. As a result, Fort Irwin did not conduct the required system analysis. Although RFAAP personnel performed the system analysis, they did not identify any control weaknesses in the contractor’s record-keeping process.

At Fort Irwin, the contractor recorded a bench valued at \$374.85 as \$374,085 in its Costpoint Property Management system. According to contractor personnel, it was merely a typographical error. Fort Irwin had developed a system analysis plan that could have detected this type of error, but Fort Irwin management did not approve the plan and, therefore, it was not implemented. Thus, Fort Irwin did not validate the integrity of data recorded in the contractor’s property management system. In another instance, at RFAAP, we identified a \$30 recording error in the contractor’s records that listed an air vibratory feeder as \$17,663 instead of \$17,633. Those errors and discrepancies remained undetected until our audit because a contractor employee had performed the data-entry function without receiving adequate supervisory review.

According to DoD Manual 4161.2-M, performing a system analysis helps identify the need for improved property management practices. However, installation officials at RFAAP and Fort Irwin were not able to identify that the contractor’s property records were not accurate. As a result, by not conducting a system analysis at Fort Irwin and not providing adequate supervisory review at RFAAP and Fort Irwin, installation officials may not be able to determine if the contractor is efficiently managing Government property.

Identification and Transfer Documentation

Army Federal Acquisition Regulation Supplement (AFARS) 5145.391, "Documentation of Government Property in Solicitations and Contracts," October 2001, requires contracts to contain identification of all GFP, including nomenclature, quantity, acquisition value, and, where applicable, model number, serial number, and year of manufacture.

Furthermore, the AR 735-5, "Property Accountability – Policies and Procedures for Property Accountability," February 2005, requires the Army to transfer accountability of Government property using DD Form 1149 or DA Form 3161, "Request for Issue or Turn-In." However, when the RFAAP and Fort Irwin transferred assets, they did not have either the specific identification information or the proper transfer documentation.

For example, Fort Irwin listed GFP in the Technical Exhibits section of the contract but did not include information that would specifically identify the property. For 21 of 30 assets, Fort Irwin did not have a DD Form 1149 or DA Form 3161 to support transfer of accountability to the contractor. As a result, RFAAP and Fort Irwin did not have adequate supporting documentation (such as a contract Technical Exhibit or transfer documentation) for assets held by the contractors to substantiate the assets' acquisition cost recorded in their financial reporting database.

Contract Modifications

RFAAP and Fort Irwin did not issue contract modifications to update periodic changes, such as additions and deletions, to Government property, in accordance with AFARS. AFARS Subpart 5145.3, "Providing Government Property to Contractors," October 2001, states that contracting officers must ensure that changes to Government property made over time be reflected by modification to the contract. However, contracting officers at RFAAP and Fort Irwin did not modify contracts to document issued or returned Government property. Some Army personnel said that they were not aware of the requirement or did not implement the requirement. As a result, the contracting records did not accurately reflect changes to Government property. In addition, not having a clear record of property made available to the contractor could limit RFAAP and Fort Irwin officials' ability to track and use assets for support of Army operations.

Conclusion

Adequate internal controls are critical to ensuring proper financial reporting and property accountability. The lack of adequate internal controls over financial reporting could lead to misstated financial statements. The lack of adequate internal controls over property accountability could lead to unauthorized use, destruction, or loss of property; and could affect the ability to track and use assets for support of Army operations.

The Army was responsible for providing reliable financial information. However, RFAAP and Fort Irwin did not report all of their capital assets in the possession of contractors, did not take depreciation on capital assets, and did not adequately support financial data. As a result, the Army financial statements were misstated.

Contractors were accountable for Government property in their possession. The Army was responsible for providing adequate oversight to ensure that contractors safeguarded Government property from unauthorized use, destruction or loss and maintained property records that produce reliable information when needed. However, RFAAP and Fort Irwin did not provide adequate oversight. They did not perform system reviews for record-keeping, physical inventory, and identification of Government property, and did not follow guidance when transferring property accountability at the time of contract award and during the course of contract performance. As a result, property records were inaccurate and incomplete, and property accountability was not appropriately established or transferred for all Government property furnished to contractors.

Army internal controls over Government property in the possession of contractors were not effective to: provide reliable financial data for decision-making; safeguard Government property; and track and use assets for Army operations support. Therefore, the Army needs to strengthen controls over Government property in the possession of contractors by implementing our recommendations.

Management Comments on the Finding and Our Response

Army Materiel Command Comments

The Executive Deputy to the Commanding General, Army Materiel Command (AMC) agreed with the finding regarding the internal control weaknesses identified at RFAAP. Specifically, the Executive Deputy stated that AMC had identified property accountability as a material weakness at its installations during internal reviews conducted in FY 2008. Further, the Executive Deputy stated that AMC has begun corrective actions, including the award of a new contract at RFAAP and the implementation of a Command Supply Discipline Program, both to occur by the end of FY 2009.

Our Response

We commend AMC for taking actions to improve internal controls over property accountability at AMC installations. Implementation of an aggressive Command Supply Discipline Program will enable AMC to improve property accountability and financial reporting at its installations and correct internal control weaknesses.

Recommendations, Management Comments, and Our Response

Revised Recommendation. As a result of management comments, we revised Recommendation 1.a. to clarify our intention that contracts should include procedures for contractors to provide information to PBOs or Property Administrators, who can update their property accounting system to ensure financial compliance for Government property in their care.

1. We recommend that the Army Materiel Command and the Army Installation Management Command direct contracting offices to:

a. Write contracts to require contractors to provide updates to capital assets in their property system to PBOs or Property Administrators for inclusion in the Army property system to ensure financial compliance with the DoD Financial Management Regulation and Army Regulation 710-2.

Management Comments

The Executive Deputy, AMC did not agree with the draft recommendation, stating that although AR 710-2 states that DPAS is the DoD system of choice for accounting for property, plant, and equipment, it does not dictate DPAS for contractor use. In addition, AMC explained that FAR 45.103 states that agencies will not generally require contractors to establish property management systems that are separate from a contractor's established system used to account for and manage contractor-owned property. The Executive Deputy, AMC stated that AMC would ensure compliance with the use of DPAS by having PBOs and Property Administrators report general property, plant, and equipment over \$100,000.

The Executive Deputy, AMC expressed concern that current Army regulations, the FAR, or the Regulatory Flexibility Act would not support the recommendation. She added that to depart from that philosophy to find a solution for tracking property might require approval from the new Office of Information and Regulatory Affairs per the Paperwork Burden Act. The Executive Deputy, AMC stated that, if necessary, AMC would participate with the Department of the Army and the DoD to re-examine how Army property accountable systems can facilitate the financial aspects of reporting.

The Army Installation Management Command did not comment on the recommendation.

Our Response

Although AMC disagreed, we considered AMC's comments were partially responsive. We agree with the AMC position that contracts should not require contractors to use DPAS. We also agree that requiring PBOs and Property Administrators to report GFP over \$100,000 in DPAS will help ensure financial compliance. We understand the AMC concerns, but we would like to clarify that those concerns do not meet the intent of the recommendation. However, our audit identified that contractors were not providing information on capital assets to PBOs and Property Administrators for inclusion in DPAS. We revised our recommendation to clarify our intention that management implement procedures to ensure that updates to capital asset information in the contractor's property system are provided to PBOs and Property Administrators for inclusion in the Army system of choice.

We request that AMC provide additional comments on the revised recommendation and that the Army Installation Management Command provide comments on the final report by July 20, 2009.

b. Provide oversight to ensure recording, labeling, inventory, and accounting for Government property in the possession of contractors, to include the retention of related supporting documentation.

Management Comments

The Executive Deputy, AMC agreed with the recommendation, stating that AMC would ensure oversight through the Command Supply Discipline Program, which will assess each AMC installation at least once every 2 years beginning in October 2009.

The Army Installation Management Command did not comment on the recommendation.

Our Response

The AMC comments were responsive. We request that the Army Installation Management Command provide comments on the final report.

c. Conduct a system analysis of contractor’s property control system, as required by DoD Manual 4161.2-M.

Management Comments

The Executive Deputy, AMC agreed with the recommendation, stating that AMC would provide assistance to RFAAP to ensure the review is sufficient and in accordance with DoD Manual 4161.2-M. AMC planned to complete the action by October 2009.

The Army Installation Management Command did not comment on the recommendation.

Our Response

The AMC comments were responsive. We request that the Army Installation Management Command provide comments on the final report.

d. Write contracts to require contractors to maintain sufficient property information to identify Government-furnished property and to establish contractor property accountability in accordance with the Army Federal Acquisition Regulation Supplement 5145.391.

Management Comments

The Executive Deputy, AMC agreed with the recommendation, stating that AMC would conduct a review of contracts to ensure the requirement is being met. AMC further stated that it would take immediate action for future property transfers and the new contract for RFAAP, which will be awarded in late FY 2009.

The Army Installation Management Command did not comment on the recommendation.

Our Response

The AMC comments were responsive. We request that the Army Installation Management Command provide comments on the final report.

e. Issue contract modifications to reflect periodic changes in Government property in the possession of contractors in accordance with the Army Federal Acquisition Regulation Supplement 5145.3.

Management Comments

The Executive Deputy, AMC agreed with the recommendation, stating that the Command Supply Discipline Program would include oversight for contract modifications and that action would begin immediately.

The Army Installation Management Command did not comment on the recommendation.

Our Response

The AMC comments were responsive. We request that the Army Installation Management Command provide comments on the final report.

2. We recommend that the Army Materiel Command and the Army Installation Management Command:

a. Direct the installation command to certify that year-end property financial data are accurate, complete, and current.

Management Comments

The Executive Deputy, AMC agreed with the recommendation, stating that AMC would complete reviews of policy and procedures for financial certification by October 2009.

The Army Installation Management Command did not comment on the recommendation.

Our Response

The AMC comments were responsive. We request that the Army Installation Management Command provide comments on the final report.

b. Redefine the roles and responsibilities of the installation property book office to include the function of financial reporting of Government property.

Management Comments

The Executive Deputy, AMC agreed that adding the financial function to PBO and Property Administrator roles would increase the Command's ability to accurately report financial data. The Executive Deputy also stated that AMC would complete training programs for civilian PBOs and Property Administrators by December 2009.

The Army Installation Management Command did not comment on the recommendation.

Our Response

The AMC comments were responsive. We request that the Army Installation Management Command provide comments on the final report.

- 3. We recommend that the Army Materiel Command and the Army Installation Management Command develop an approach to enforce the use of standard transfer documents when transferring accountability of Government property to and from contractors in accordance with Army Regulation 735-5.**

Management Comments

The Executive Deputy, AMC agreed with the recommendation, stating that reviews of property transfers would be part of the Command Supply Discipline Program and would begin by October 2009.

The Army Installation Management Command did not comment on the recommendation.

Our Response

The AMC comments were responsive. We request that the Army Installation Management Command provide comments on the final report.

Appendix A. Scope and Methodology

We conducted this performance audit from October 2007 through February 2009 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. As of February 2009, the conditions and causes identified in this report remain relevant. According to management at RFAAP and Fort Irwin, there have been no changes in the processes, controls, and contract that affect GFP since the completion of the audit.

We performed an audit of databases, processes, and regulatory requirements for financial reporting and property accountability of Government property in the possession of contractors. We conducted the audit at RFAAP, Virginia, from October 15 through 26, 2007, and at Fort Irwin, California, from November 27 through December 6, 2007. At those sites, we tested the existence, completeness, and valuation of Government property.

For our methodology, we selected two major commands, based on the highest and median dollar amount of GFP recorded in DPAS. We selected the Army Materiel Command because it had the highest dollar amount of GFP and the U.S. Army Forces Command because it had the median dollar amount of GFP. Next, we selected RFAAP from the Army Materiel Command because it had the highest dollar amount of GFP recorded in DPAS, and we selected Fort Irwin from the U.S. Army Forces Command because it had the third highest dollar amount of GFP recorded in DPAS. Finally, although the Army divided Fort Irwin into two commands (the National Training Center and Fort Irwin Garrison), the DPAS database did not separate it into two commands. Therefore, we judgmentally selected the Garrison Command, under the Installation Management Command, for review.

For our universe, we requested GFP records for sample selection from RFAAP and Fort Irwin, and they provided official Government property records on September 13, 2007, and on November 8, 2007, respectively. From those universes, we judgmentally selected samples for existence and valuation tests. During our existence tests at the sites, we judgmentally selected samples from the floor to test for completeness. During our site visits, we also discovered that contractors did not maintain a database for GFP that was separate from contractor-acquired property and that the data provided for sampling actually contained both types of Government property in the possession of contractors. Therefore, we expanded the audit scope to include contractor-acquired property.

We developed review checklists based on criteria established in the FAR, DFARS, DoD FMR, DoD instructions and manuals, and Army regulations. We interviewed the Army PBO, property administrators, contracting officers, accounting staff, and contractor personnel; and examined property records and supporting documentation, including contracts, transfer documents, hand receipts, inventory records, and accounting records.

We also reviewed standard operating procedures for the Army contractors and observed the contractors' processes for receiving and recording Government property.

We compared results of our examination and observation to the established criteria to assess the Army internal controls over financial reporting and accountability of Government property in the possession of contractors.

Use of Computer-Processed Data

To achieve the audit objective, we used data that originated from a Microsoft Access database, the Costpoint Property Management system, DPAS provided by RFAAP and Fort Irwin, and the Defense Finance and Accounting Service. We used the data to determine the sample of Government property for our review. To determine the data validity of our sample amounts, we compared the system data to source documents such as contracts, transfer documents, hand receipts, inventory records, and accounting records. The assessment indicated that data were sufficiently reliable to meet our audit objectives.

Use of Technical Assistance

The Quantitative Methods Division (now the Quantitative Methods and Analysis Directorate) of the Department of Defense Inspector General (DoD IG) provided assistance. The Division selected a random sample based on the data provided in the universe, which became the basis for our judgmental sampling.

Prior Coverage

During the last 5 years, the DoD IG and the Army Audit Agency (AAA) have issued four reports discussing the management of Government-furnished property and systems for property accountability and financial reporting. Unrestricted DoD IG reports can be accessed at <http://www.dodig.mil/audit/reports>. Unrestricted Army Audit Agency reports can be accessed over the Internet at <http://www.aaa.army.mil/reports.htm>.

DoD IG

DoD IG Report No. D-2006-046, "Technical Report on the Defense Property Accountability System," January 27, 2006

DoD IG Report No. D-2005-092, "Report on Defense Property Accountability System Controls Placed in Operation and Test of Operating Effectiveness for the Period September 1, 2004 through April 30, 2005," July 7, 2005

AAA

AAA Audit Report A-2005-0126-FFE, "Management of Government-Furnished Property-U.S. Army Garrison Fort Hood, Texas, Validation of Property Book and Unit Supply Enhanced System," March 4, 2005

AAA Audit Report A-2004-0473-FFG, "Validation of Property Book and Unit Supply Enhanced System-Requirements Followup," September 8, 2004

Appendix B. Glossary of Technical Terms

Accountability. Accountability is the obligation imposed by law, lawful order, or regulation, accepted by an organization or person for keeping accurate records, to ensure control of property, documents, or funds with or without physical possession. The obligation, in this context, refers to the fiduciary duties, responsibilities, and obligations necessary for protecting the public interest; however, it does not necessarily impose personal liability upon an organization or person.

Best Practices. Best practices are techniques that agencies may use to help detect problems in the acquisition, management, and administration of service contracts. Best practices are practical techniques gained from experience that agencies may use to improve the procurement process.

Capitalization. Capitalization is to record and carry forward into one or more future periods any expenditure the benefits of which will then be realized. The DoD capitalization threshold for General Property, Plant, and Equipment, except for real property, is currently \$100,000.

Completeness. Assertions about completeness address whether all transactions and accounts that should be presented in the financial statements are so included. For the purpose of this report, completeness addresses whether all Government property found on the floor at the time of our observation was recorded in the property accountability and financial reporting systems, as applicable.

Existence. Assertions about existence or occurrence address whether assets or liabilities of the entity exist at a given date and whether recorded transactions have occurred during a given period. For the purpose of this report, existence addresses whether Government property recorded in the contractor's property management system, which serves as the official Government property record, physically exists at the time of our observation.

Government Property. Government property means all property owned or leased by the Government and includes both GFP and contractor-acquired property.

- **Government-furnished Property.** GFP is property in the possession of, or directly acquired by, the Government and subsequently furnished to the contractor for performance of a contract.
- **Contractor-acquired Property** Contractor-acquired property is property acquired, fabricated, or otherwise provided by the contractor for performing a contract and to which the Government has title.

Internal Controls. Internal controls are the plan of an organization and all methods and measures adopted within an organization to safeguard its assets, check the accuracy and reliability of its data, promote operational efficiency, and encourage adherence to prescribed managerial policies.

Physical Inventory. Physical inventory is the verification of property existence, location, and quantity.

Property Management. Property management is a monitoring and control function that ensures that organizational processes related to the life cycle of property: (1) support organization objectives, (2) represent sound business practice, and (3) are compliant with applicable standards, policies, regulations, and contractual requirements.

Valuation. Assertions about valuation or allocation address whether asset, liability, equity, revenue, and expense components have been included in the financial statements at appropriate amounts. For the purpose of the report, valuation addresses whether financial records of Government property were accurate in terms of acquisition costs and depreciation.



REPLY TO
ATTENTION OF:

DEPARTMENT OF THE ARMY
HEADQUARTERS, U.S. ARMY MATERIEL COMMAND
9301 CHAPEK ROAD
FORT BELVOIR, VA 22060-5527

AMCIR

23 March 2009

MEMORANDUM FOR Inspector General, Department of Defense, [REDACTED] 400 Army
Navy Drive, Arlington, VA 22202-4704

SUBJECT: Comments to DODIG Draft Report – Internal Controls Over Government Property in the
Possession of Contractors At Two Army Locations (D2007-D000FH-0231.000) (D0727)

1. The U.S. Army Materiel Command (AMC) has reviewed the subject draft report and has enclosed specific AMC comments addressing the eight recommendations.
2. Regarding the internal control weakness identified at Radford, AMC concurs as AMC has identified property accountability as a material weakness at AMC Installations based on an internal review conducted in FY08. The findings at Radford are not extensive and corrective actions have already begun, many of which will be addressed with the award of a new contract this Fiscal Year. Further, AMC is taking active measures to fully implement an aggressive Command Supply Discipline Program by the end of FY 2009 to ensure property accountability and financial reporting are no longer a material or internal control weakness.
3. The AMC point of contact is [REDACTED]

Encl

KATHRYN A. CONDON
Executive Deputy to the
Commanding General

COMMAND COMMENTS
D2007-D000FH-0231.000

Draft Report – Internal Controls Over Government Property in the Possession of Contractors At Two Army Locations

Objectives: Evaluate the Department of Army (DA) internal controls over Government-furnished property. Specifically, DODIG examined databases and processes at the Radford Army Ammunition Plant in Virginia and Ft. Irwin in California that accounted for existence, completeness, and valuation of Government property in the possession of contractors. Further, DODIG determined whether DA clearly defined its requirements for Government-furnished property.

Conclusion: Army internal controls over its processes and databases did not accurately account for the existence, completeness, and valuation of Government property in the possession of contractors at Radford Army Ammunition Plant, Virginia and Ft. Irwin, California. Specifically, internal controls were not effective for financial reporting and accountability of Government property, valued at \$169.6 million in the possession of contractors.

Further, ineffective controls resulted from noncompliance with DOD and Army guidance for financial reporting, contract administration, and property accountability; and insufficient oversight processes of Government property. Therefore, the Army financial statements and databases were misstated. In addition, the two Army locations may not be able to safeguard Government property from unauthorized use, destruction, or loss.

1. We recommend that the Army Materiel Command direct contracting offices to:

a. Write contracts to require contractors to update and use of the Army system of choice to account for Government property in contractor possession to ensure financial compliance with DOD Financial Management Regulation and Army Regulation 710-2.

AMC Comments: Non-Concur. AR 710-2 states that the Defense Property Accountability System (DPAS) is the DOD system of choice for accounting for property, plant, and equipment (PPE) for installations and non-deployable activities. The regulation does not dictate DPAS for contractor use. AMC will ensure compliance with the use of DPAS by property book officers/administrators to report general PPE over the value of \$100,000 as required for Chief Financial Officer (CFO) purposes when the contractor is not using DPAS.

AR 710-2 excerpt:

1–13. Defense Property Accountability System (software program)

The Defense Property Accountability System (DPAS) is a DOD Deputy Secretary of Defense mandated property accounting system for enabling integrated logistics and financial accounting required by the Chief Financial Officer's (CFO) act.

a. DPAS will be fielded to installations and non-deployable activities maintaining property books, and enables the reporting of general property, plant, and equipment costing over the threshold of \$100,000 for CFO purposes.

- b. DPAS can record, track, calculate depreciation and facilitate the annual reporting of general property.

In addition, AR 735-5 paragraph 2-5 states that the Property Book Office will create and maintain a GFP asset listing for fiduciary reporting purposes. The Federal Acquisition Regulation (FAR) also states that as a practice, the contractor should be allowed to use their property management system.

FAR 45.103 excerpt:

General. b) Agencies will not generally require contractors to establish property management systems that are separate from a contractor's established procedures, practices, and systems used to account for and manage contractor-owned property.

AMC has also reviewed the 15 March 2007 Federal Register Notice that set forth the new FAR property rules. Our conclusion is that current Army and Federal acquisition regulations will not support this recommendation. The drafting team, as stated in the notice, specifically considered the use of government mandated systems but rejected this approach. In addition, per the Regulatory Flexibility Act, Government is expected to reduce the burden on small businesses by making compliance with regulations as inexpensive as possible and require as few labor hours as possible. Should the Army or DOD desire to depart from that philosophy by imposing a particular solution for tracking property that affects more than 10 businesses, a new Office of Information and Regulatory Affairs approval must be obtained per the Paperwork Burden Act. Given that the entire rule is based on use of commercial practices and OMB Circular A-119, which also emphasizes the use of industry standards, such approval is unlikely. However, we recognize a resource and compliance shortfall with the PBOs not maintaining a separate property account in DPAS for GFP just for financial reporting purposes. AMC will participate with DA and DOD if needed, in an effort to re-examine the way ahead for Army property accountable systems to facilitate the financial aspects of reporting.

- b. Provide oversight to ensure recording, labeling, inventory, and accounting for Government property in the possession of contractors, to include the retention of related supporting documentation.

AMC Comments: Concur. Segregation and proper labeling is a standard requirement specified in DOD Manual 4161.2. AMC will ensure oversight of this function through the implementation of the AMC Command Supply Discipline Program (CSDP) which will assess each AMC installation at least once every 2 years. Reviews begin in Oct 09.

- c. Conduct system analysis of contractor's property control system, as required by DOD Manual 4161.2-M.

AMC Comments: Concur. Radford AAP conducts annual reviews however it was found that the reviews were not sufficient to determine if the contractor was efficiently managing government property. AMC will provide assistance to Radford AAP as needed to ensure the review is sufficient and in accordance with DOD Manual 4161.2. Action will be taken by Oct 2009 in conjunction with award of the new contract at Radford AAP.

- d. Write contracts to require contractors to maintain sufficient property information to identify Government-furnished property and to establish contractor property accountability in accordance with the Army Federal Acquisition Regulation Supplement 5145.391.

AMC Comments: Concur. AMC will conduct a review of contracts to ensure this requirement is being met. Radford AAP will ensure any future transfer documentation has the minimum requirements established in AFAR Supplement 5145.391. If for some reason acquisition costs are not available, any recorded amounts will be properly justified and documented with appropriate signatures. Immediate action will be taken for future transfers and the new contract to be awarded in late FY 2009 will include this requirement.

e. Issue contract modifications to reflect periodic changes in Government property in the possession of contractors in accordance with the Army Federal Acquisition Regulation Supplement 5145.3.

AMC Comments: Concur. AMC will provide oversight of this recommendation through the CSDP. Immediate action will be taken and a review of compliance for all AMC activities as part of the CSDP.

2. Recommend that the Army Materiel Command and Army Installation Management Command:

a. Direct the installation commander to certify that year-end property financial data are accurate, complete, and current.

AMC Comments: Concur. It is each Commander's responsibility to ensure property data is accurate, complete, and current. AMC will complete review of policy and procedures for financial certification by Oct 2009.

b. Redefine the roles and responsibilities of the installation property book office to include the function of financial reporting of Government property.

AMC Comments: Concur. AMC will review the training of civilian property book officers and administrators. AMC supports adding the financial function to property book officer/administrator roles which will enable the Command's ability to accurately report financial data. Training program will be completed by Dec 2009.

3. Recommend that the Army Materiel Command and the Army Installation Management Command develop an approach to enforce the use of standard transfer documents when transferring accountability of Government property to and from contractors in accordance with Army Regulation 735-5

AMC Comments: Concur. AMC activities should follow regulatory requirements for property transfers. AMC will review the compliance as part of CSDP. Reviews will begin by Oct 2009



Inspector General Department of Defense

