# Testimony

STATEMENT OF
ELEANOR HILL
INSPECTOR GENERAL, DEPARTMENT OF DEFENSE
BEFORE THE SUBCOMMITTEE ON
GOVERNMENT MANAGEMENT INFORMATION TECHNOLOGY
COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT
HOUSE OF REPRESENTATIVES
ON DEPARTMENT OF DEFENSE FINANCIAL MANAGEMENT

Report Number 98-118 DELIVERED: APRIL 16, 1998

Office of the Inspector General
Department of Defense

Hold for Release
Until Delivery
Expected 10:00 a.m.
April 16, 1998

**Statement by**

**Ms. Eleanor Hill**

**Inspector General**

**Department of Defense**

**Before the**

**Subcommittee on Government Management**
**Information and Technology**

**Committee on Government Reform and Oversight**

**House of Representatives**

**on**

**Department of Defense Financial Management**

**April 16, 1998**

Mr. Chairman and Members of the Committee:

Thank you for the opportunity to discuss with you today financial management in the Department of Defense, with emphasis on the Department's continued efforts to achieve compliance with the Chief Financial Officers Act and related statutes. As you know, I testified before this committee on November 14, 1995, and at that time outlined the significant impediments hampering the preparation of auditable annual financial statements by the Department. There has been little controversy about what those impediments are. The Department has generally agreed with the huge number of audit findings on the subject. Its management representation letters, annual management control assurance statements, and other reports to the Office of Management and Budget and the Congress have acknowledged the scope of the problem.

The Department's accounting systems and financial reporting practices mirrored its overall management philosophy during the 1950's through 1980's. Most DoD business processes--acquisition, inventory management, maintenance, training, and many others--were decentralized; controlled in theory by elaborately detailed rules and regulations; developed unilaterally by organizations operating within their own functional "stovepipe" with insufficient coordination with other stakeholders; and often labor intensive despite the use of many thousands of automated systems. In the finance and accounting area, each Military Department operated dozens of systems; data element standardization was never

effectively enforced; DoD accounting policies were enunciated in a Handbook whose precepts were not mandatory and therefore were widely ignored; and the primary focus of financial reporting was on funds control, not on providing the full range of financial data needed by managers. In retrospect, it is remarkable how infrequently the DoD accounting community was asked questions along the lines of how much does it cost to run a base, fill a requisition or operate a warehouse.

With the end of the Cold War and the imposition of severe DoD budget constraints, the Department and the Congress recognized the need to reform the entire range of DoD business practices. For nearly ten years, the Department has been engaged in reinventing all of those processes simultaneously. While indeed much has been accomplished, much remains to be done in all aspects of the Department's operations. Last month I testified, for example, before a Senate committee that was evaluating the impact of acquisition reform, about problems in pricing for spare parts, and opportunities for further acquisition process improvements.

Nearly all of my office's audit and evaluation work directly relates to the Department's high risk areas and strategic management reform goals. Therefore we have an overview of the relative progress being made in reengineering each DoD functional area. Although each of those areas entails tremendous complexity and many challenges, it is easier to enumerate or quantify progress

in most other areas than in finance and accounting. This is frustrating to everyone--the Congress, OMB, DoD managers, the comptrollers, and the auditors.

My office has issued 181 audit reports on finance and accounting matters since I last testified before you, and only a handful have been good news. Some examples of our recent reports are summarized at Attachment 1. The Military Department audit agencies have also done a substantial part of the CFO audit work and produced numerous reports. Although tens of billions of dollars' worth of auditor-recommended adjustments are being made annually to financial statements and hundreds of other audit recommendations are being accepted, I cannot yet report to you that the Department has successfully corrected the many shortcomings in its accounting and financial systems.

The financial statement data for most DoD funds remain unreliable and essentially not in condition for audit. In accounting terms, the situation still can best be described as a general lack of effective internal management controls. Consequently, we and the Service audit organizations were unable to give audit opinions on the financial statements for either the DoD-wide consolidated statements or all but one of the major fund statements for FY 1997. We are still working on the Military Retirement Trust Fund statements, which probably will merit an

unqualified (clean) opinion and be the only exception to the list of disclaimers. A complete listing of the audit opinions is at Attachment 2 to this statement.

GENERAL FUNDS

The primary reason for disclaimers of opinion on all DoD general fund financial statements for FY 1997 has not changed since the November 15, 1995, testimony; the accounting systems supporting DoD general funds cannot compile and report accurate and reliable information. Accounting systems supporting DoD general funds continue to lack integrated, double-entry, transaction-driven general ledgers to compile and report reliable and auditable information. The information is not auditable because the accounting systems cannot produce an audit trail of information from occurrence of a transaction through its recognition in accounting records and ultimately to the general fund financial statements. Not all information from the audits of the FY 1997 financial statements is available yet, but it is apparent that, as in previous years, DoD made huge numbers of adjustments, many of which were unsupported. For example, the DFAS Indianapolis Center made $350 billion of unsupported adjustments to make the FY 1997 Army General Fund general ledger accounts match the corresponding status of appropriations data.

Because of the accounting systems' inadequacies, auditors have not been able to obtain sufficient evidence or apply other auditing procedures to satisfy themselves as to the fairness and accuracy of the data reported on DoD general fund financial statements. Until accounting systems with integrated, double-entry, transaction-driven general ledgers are developed to compile and report information, auditors will remain largely unable to determine whether valid transactions are properly recorded, processed, and summarized. This is a significant long-standing scope limitation that will likely continue to cause auditors to disclaim opinions on the DoD general fund financial statements. The Department does not expect to see most of the necessary systems fully in operation before 2003.

Since 1995 there have been various other developments affecting the general funds. Some are positive and others present mixed signals.

- The Defense Property Accountability System (DPAS), which was proposed as the answer to unreliable reporting of real and personal property, is being fielded, but has fallen short of expectations. Specifically, DPAS only captures about a quarter ($182 billion out of $773 billion reported in FY 1996) of real and personal property and does not completely address the systemic weaknesses it was intended to correct.

- The General Accounting Office and DoD auditors performed a coordinated review of DoD mission assets during the FY 1997 CFO audit. Mission assets, more properly referred to as National Defense Property, Plant and Equipment, are weapon systems and other equipment used in the performance of actual military operations. Examples would be aircraft, ships, trucks and jet engines. The purpose of the joint effort was to test mission assets for completeness of reporting and existence of assets. Based on a sampling methodology designed to result in a pass/fail conclusion on the categories of the items sampled, the Army and Air Force passed, while the Navy failed in three of the eleven categories.

- In FY 1997, the Army Corps of Engineers, with support from the Army Audit Agency, attempted to produce auditable Southwest Division financial statements because the Corps had completed development and implementation of its new accounting system, the Corps of Engineers Financial Management System (CEFMS), within that Division. This effort proved successful, as the auditors gave an unqualified opinion on the FY 1997 Southwest Division financial statements. The Army is completing deployment of CEFMS throughout the remainder of the Corps and is anticipating a possible favorable opinion on the FY 1999 financial statements for the Corps of Engineers, Civil Works Program.

- With extensive modifications, CEFMS serves as the basis for the Defense Joint Accounting System (DJAS). Recently the plan for DoD-wide use of DJAS has undergone major revision, however, and it is now unclear how many DoD organizations will ever use the common system.

- The Air Force, with support from the Air Force Audit Agency, attempted to produce an auditable Statement of Budgetary Resources for FY 1997. Although work continues on the statement and many challenges remain, the lessons learned from this commendable effort will provide a baseline for a potentially favorable audit opinion on the FY 1998 Air Force Statement of Budgetary Resources and for the other Services to apply in attempting to produce auditable FY 1998 Statements of Budgetary Resources.

- Two years ago, we participated in a joint effort led by the Under Secretary of Defense (Comptroller) and Principal Deputy Under Secretary of Defense (Acquisition and Technology) to deal with the long-standing problems related to control of Government-owned property in the possession of contractors. Those problems fall under two categories, accounting for the property and reengineering the related business practices--acquisition, inventory control, reutilization and disposal. In brief, one of the reasons for disclaimers of opinion on various

general fund and working capital fund financial statements is the lack of any reliable data on the depreciated value of an estimated $90 billion (acquisition value) of military property, material, tools and equipment, as well as real property in the hands of contractors. It was agreed that the appropriate accounting treatment for this property would be identified and the necessary instructions provided to the owning activities or DoD property administrators. Unfortunately, no progress has been made. Similarly, the acquisition community initiated procurement rule changes to change the practice of the Government automatically taking title to property, whether or not there was any reasonable chance of reutilization, but that effort has also bogged down.

- One of the benefits of financial statements is disclosure of liabilities. Such information should have practical applications for DoD program/budget planning. Initially, there were great concerns over criteria and methodology for estimating and reporting liabilities. Progress is being made, although this remains a difficult area. For example, the DoD-wide statements need to reflect liabilities related to military retirement health benefits. The estimate in FY 1997 was for $218 billion, which is a 100-year projection. This projection is questionable because it was based on an inadequate sample

(data from only 15 of 121 DoD treatment facilities) and the 1992-1994 data used for the projection were not updated, and used unaudited budget information.

- Another example concerns environmental costs. The reporting of estimated environmental cleanup liability is becoming more accurate, increasing from $17.9 billion for FY 1996 to $38.3 billion for FY 1997. Liabilities for disposal of hazardous waste and remediation of environmental contamination for FY 1997 remained materially understated, as a whole, primarily because an estimate for the associated liability had not been developed for major weapon systems such as aircraft, missiles, ships and submarines, as well as ammunition. DoD had not implemented the accounting standards that require recognizing and reporting environmental costs associated with weapon systems, nor had DoD provided guidance to the Services. This is an example of where the DoD management reform goals in other areas ought to dovetail with the effort to produce accurate financial statements, but the linkage is not evident to most DoD managers. In this case, DoD managers are supposed to be putting heavy emphasis on identifying and reducing the life cycle cost of weapon systems and the cost of logistics operations, including disposal. Estimating environmental cleanup liabilities should be an integral part of life cycle cost estimating. There is a very practical imperative at work here, not just an arcane accounting requirement.

## DEFENSE BUSINESS OPERATIONS FUND/WORKING CAPITAL FUNDS

One of the most touted DoD management initiatives of the 1990's was consolidating all industrial funds and stock funds into the Defense Business Operations Fund, which became the primary vehicle for financing DoD support activities such as supply, maintenance, transportation, finance, and information processing. This experiment in centralized cash management proved unsuccessful. In December 1996, the Under Secretary of Defense (Comptroller) announced that the Fund would be broken up and replaced with several Working Capital Funds. The 13 business areas under the Defense Business Operations Fund were restructured under the Military Services and the Defense agencies. This restructuring did not affect the financial reporting deficiencies that caused disclaimers of audit opinions on Defense Business Operations Fund financial statements for FY 1992 through FY 1996. Those problems include accounting system deficiencies, poor audit trails, unsupported and unverified transactions, and difficulty in determining property ownership.

For example, adjustments made to the Air Force, Transportation Command, and Joint Logistics Systems Center working capital funds by the DFAS Denver Center were not adequately supported. In FY 1996, the Denver Center made 124 adjustments for $227 billion, of which 111 adjustments for $217 billion were not supported. The

last nine adjustments made for FY 1996, which were not supported, changed the Air Force results of operations from a loss of $11 billion to a gain of $2.2 billion. For FY 1997, the Denver Center made 129 adjustments for $161 billion. We have not completed our review of the FY 1997 adjustments and cannot state at this time the number of adjustments that were adequately supported. We have noticed an improvement in the amount of documentation provided, but we are concerned with the number and types of adjustments that are made because of deficiencies in the accounting systems used. If DFAS had adequate accounting systems, many of the adjustments would be unnecessary.

The Department has developed a long-term plan to reduce the number of accounting systems from 82 to 15 that support the working capital funds and to correct the deficiencies in the systems selected for retention. Although some progress has been made in eliminating systems, few working capital fund accounting systems have implemented the U.S. standard general ledger, and no systems are fully compliant with Federal financial management system requirements and Federal accounting standards. Significant control weaknesses continue to affect the accurate reporting of inventory accounts in several working capital fund business areas. Since inventory is the primary asset reported on the working capital fund financial statements, these weaknesses will affect the fair presentation of both the individual working capital fund and DoD-

wide financial statements and prevent favorable audit opinions. We believe the most serious problems in accounting systems will remain unresolved for some time.

Financial reporting for the working capital funds should be geared to management's needs. Most of the operations financed by these funds fall under the purview of the supply, maintenance, transportation, communications and information processing communities and much of the data feeding the financial systems come from non-financial systems, especially logistics systems. This makes close cooperation among the "owners" of the financial systems and the feeder systems absolutely vital in terms of improving DoD financial reporting and designing more useful, reliable and capable systems for the future. While there is repeated acknowledgment of the need for such cooperation, we believe that the commitment of DoD managers to the goal of CFO Act compliance is, especially outside the finance and accounting community, very tenuous. Signals such as the previously mentioned inability to get all major DoD organizations to use the supposedly joint Defense Property Accountability System are disquieting. The recent consolidation of accounting system development efforts into a single Defense Financial and Accounting Service project office was a prudent decision, although we believe that closer Office of the Secretary of Defense level oversight of these systems development efforts is crucial.

We have been disappointed that the DoD Senior Financial Management Oversight Council, which was described as the capstone of the DoD financial management reform organizational structure in the Chief Financial Officer's Five Year Plan, has not met in over a year and has not discussed compliance with the CFO Act in four years. Although CFO Act issues are frequently discussed among leaders of the DoD finance and accounting organizations, the leaders of many non-finance functional areas do not appear to be actively engaged. This is not completely unexpected, in light of the sheer number of management challenges facing the Department and the resultant conflicting priorities.

## AUDITING FINANCE AND ACCOUNTING OPERATIONS

Although there is widespread skepticism in the DoD concerning the value of financial statements themselves, the certainty of the annual financial audit has contributed to increased attention to problems that may not in all cases be material to DoD financial statements, but are important in achieving sound financial management. Such problems include disbursements that cannot be matched to original obligations, untimely purging of invalid obligations, overpayments to contractors, lack of attention to maintaining appropriation integrity when making progress payments, the Year 2000 computing problem, and vulnerability to computer tampering and fraud.

Unfortunately, financial statement audits are not necessarily the most efficient audit approach to identifying the scope and causes of such problems. For truly effective oversight, the financial statement audits required under the CFO Act need to be augmented with a robust annual program of operational audits of finance operations. Due to the combination of the downsizing of my office (58 percent of non-CFO audit teams must be eliminated by 2002 under current plans), the high demand for audit support in other DoD high risk areas, and the highly labor intensive nature of financial statement audits for huge funds with many assets, our overall coverage in the finance and accounting area is bordering on inadequate. For example, the Defense Commissary Agency is the tenth largest food retailer in the United States in sales. We audited the FY 1997 Financial Statements with a team of four auditors, which was feasible only because the underlying systems and controls were in such a state that no more than limited audit tests were considered necessary.

We have earmarked 20 audit teams to CFO Act work, which is a major commitment in light of all other priorities. By 2002, those 20 teams will be a full one-third of our entire audit staff. Although the DoD audit community is proud of its strong commitment to meeting the CFO audit challenge, we feel that we are losing ground in terms of having the resources to get the job done. Over the past several years, our audit reports on such matters as the “M” accounts, problem disbursements, and DoD compliance with budget

authorization and appropriation act mandates have been widely used by DoD managers and Congress. By FY 1998, we are already unable to offer as much insight into such matters as we did previously, and this trend will become even more marked if our downsizing continues.

It is perhaps not well understood that CFO Act audit requirements are increasing for a variety of reasons:

- First, the Government Management Reform Act expanded the mandatory audit requirements to cover all DoD funds.

- Second, guidance from the Federal Accounting Standards Advisory Board and OMB increased the number of statements to be provided for each fund from 3 to 8. This will create various new reconciliation challenges for both the preparers and auditors of these statements.

- Third, under current plans, the number of DoD reporting entities (funds for which financial statements, management representation letters, and legal representation letters are prepared) has grown from 11 in 1995 to 20 in 1998. We have recently advised the Under Secretary of Defense (Comptroller) that it is impossible to execute a plan for separate audit opinions for so many reporting entities, given our resource constraints. In

addition, we need to put top audit priority on focusing on those major areas that most materially affect the DoD-wide consolidated statements and the Government-wide statements. We have proposed a more practical approach involving separate audit opinions for 13 reporting entities.

- Fourth, concerns regarding the security of automated financial systems have become much more prominent as the DoD has identified the broad overall threat posed to all of its systems by computer hackers. According to estimates from the Defense Information Systems Agency, DoD systems are attacked approximately 250,000 times per year.

- Fifth, the ability of both the finance and accounting automated systems and the other systems with which they exchange data to compute accurately after January 1, 2000, is a serious concern. Across the board, the DoD audit community now has about 150 auditors working on the “Y2K” problem, and this commitment is likely to grow.

- As DoD funds reach the point where clean audit opinions are within reach, the scope and intensity of transaction testing by the auditors may increase. At the present time, audit scope is limited in many cases because of the state of the records.

## NEED TO SIMPLIFY ACCOUNTING

Another frustration that is widely evident in the DoD at the present time concerns the excessive complexity of DoD accounting. It is ironic that there is strong support for streamlining organizations, regulations and processes, yet there is dogged resistance to the concept of simplifying our accounting.

The Department is moving forward in reducing the number of accounting systems, which stood at 324 in 1991 and is down to 122 now. The goal is 23 by FY 2003. Whether we have hundreds of systems or just a few, however, there will still be tremendous complexity, workload, and vulnerability to errors unless we also reengineer the accounting structure itself.

The Department's accounting methods were designed decades ago to maintain the integrity of each of the tens of thousands of accounts maintained by the DoD in what is undoubtedly the most complicated chart of accounts in the world. This multiplicity of "colors of money" is a root cause of the formidable DoD problems with the accuracy of accounting data, the complexity of our contracts, the difficulty of properly managing disbursements and progress payments, the high overhead costs of DoD budget and accounting operations, and the considerable restrictions on the flexibility of managers to shift funds quickly to meet contingencies. Millions of documents must contain at least one,

and in some cases, many accounting classification codes that typically have from 46 to 55 characters each. Compare 16 characters used for a commercial credit card to a typical Navy fund cite:

17x1611 1936 026 54002 3 068572 ID 000151 000560852000

We believe that the DoD and Congress ought to reconsider the need for so many discrete appropriations and subaccounts. These kinds of issues are seldom considered in the context of management reform, but we believe that any streamlining of DoD financial management requirements would considerably assist managers in cutting overhead costs throughout the Department.

SUMMARY

During my previous testimony, I recounted that as long as 213 years ago, the Congress and the military establishment had been debating the need for adequate audit trails for military expenditures. Unfortunately, we are now going on 217 years and the Department still cannot provide you an acceptable accounting of expenditures. The DoD audit community is very much aware of the explicit mandates on this subject and we will continue to do all we can to move the Department forward to full compliance with the CFO Act.

# EXAMPLES OF FY 1998 OFFICE OF INSPECTOR GENERAL, DOD, REPORTS ON FINANCE AND ACCOUNTING

Report No. 98-075, Distribution Depot Revenues, February 13, 1998. The Distribution Depot business area was not reimbursed for all transportation and container consolidation point services. Customers were only billed $126 million of the $275 million of costs incurred. As a result, the Distribution Depot business area lost approximately $150 million in FY 1996, and the lack of full reimbursement was not disclosed in the FY 1996 financial statements. Also, the Distribution Depot business area continued to provide services to customers in advance of, or in excess of the amount of, funded orders. Cumulative unfunded services ranged from $1 million to $75.4 million per month during the 15-month period ended December 31, 1996. As a result, the Distribution Depot business area experienced cumulative cash disbursements that exceeded cumulative cash collections by as much as $181.4 million during FY 1996. Cash shortages had to be covered by other Defense Business Operations Fund (DBOF) sources. These kinds of problems cause pricing distortions and complicate budget planning.

Report No. 98-072, Defense Business Operations Fund Inventory Record Accuracy, February 12, 1998. The audit assessed the accuracy of the perpetual inventory records for on-hand inventory maintained by the DoD inventory control points and retail storage activities. The audit was limited because DoD management had not developed and executed a DBOF-wide sample; we developed a sample to test inventory record accuracy.

The inventory records were not accurate. An estimated 15.8 percent, or about one of every six inventory records represented by our sampling, were wrong. The errors caused individual inventory records to be misstated (overstated and understated) by an estimated $3.9 billion. The net misstatement resulting from those errors was an estimated $336.3 million understatement of the $89 billion of on-hand inventory reflected in the FY 1996 financial statements. The inaccurate records greatly limited the reliability of the financial data. Inaccurate inventory records also distorted the reports used by inventory managers who made decisions to buy materiel. Additionally, inaccurate records can reduce the effectiveness of logistics support when military customers urgently need inventory.

The DoD inventory control points and retail storage activities did not implement a plan to conduct an annual statistical sample of the FY 1996 Defense Business Operations Fund inventory, as required by DoD policy.

Report No. 98-060, Joint Logistics Systems Center Reporting of System Development Costs, February 3, 1998. The Center did not transfer about $1.54 billion of systems development costs, incurred through the end of FY 1996, to the depot maintenance and supply management organizations responsible for capitalizing and reporting these costs on the financial statements. Additionally, the $1.54 billion and another $460 million in development costs to be incurred through FY 1998 will be improperly charged, through the

recovery of depreciation costs, to customers of the depot maintenance and supply management business areas of the DoD Working Capital Funds. As a result, the Center's FY 1996 financial statements were materially overstated, and unless the systems development costs are properly transferred to the appropriate organizations, the financial statements for FY 1997 and beyond will continue to be overstated. Conversely, the financial statements of the organizations that receive the capital assets (that is, systems developments) will be understated. Also, unless the depreciation costs of the Center's systems developments are recorded as unfunded costs, customers of the DoD Working Capital Fund organizations that received the systems developments will have to pay again for nearly $2 billion in development costs.

Report No. 98-057, Defense Finance and Accounting Service Acquisition Program for the Electronic Document Management Program. January 27, 1998. The Defense Finance and Accounting Service (DFAS) Electronic Document Management Program will standardize document distribution, tracking, and storage. The Program is expected to improve processing time, reporting accuracy and customer service, resulting in reduced personnel costs. This audit report is one of a series on the DoD acquisition strategy for the DFAS Electronic Document Management Program and provides the results of our review of the Increment 1, Vendor Pay, life-cycle documentation. The Director, DFAS, requested that we review the implementation of the Program through the integrated product team

process and provide input during the acquisition process.

The audit indicated that the integrated product team appropriately identified cost, funding, and testing concerns that needed to be resolved before a deployment decision could be recommended. The Program Office provided a cost reconciliation document, funding information, and a schedule for testing to minimize the concerns of the integrated product teams. Management incorporated several auditor suggestions into the program plan. DFAS developed the required life-cycle documentation and subsequently received a Milestone III deployment decision, for Increment 1, Vendor Pay, on December 16, 1997.

Report No. 98-050, Defense Business Operations Fund Adjustments at the Defense Finance and Accounting Service, Denver Center, January 20, 1998. The DFAS Denver Center did not have adequate supporting documentation, in accordance with DoD 7000.14-R DoD Financial Management Regulation, for 111 adjustments totaling $217.5 billion made to the Air Force, U.S. Transportation Command, and Joint Logistics Systems Center FY 1996 DBOF account balances. The last nine adjustments made without supporting documentation brought the Air Force DBOF Results of Operations from a loss of $11 billion to a gain of $2.2 billion, and the lack of audit trails contributed to the disclaimed audit opinion for the FY 1996 DBOF financial statements. In many instances, adjustments were made to the same accounts because the adjustments were recorded incorrectly,

reversed, reestablished, decreased, or increased. However, we could not determine the validity of the adjustments because of the lack of supporting documentation.

Report 98-031, The DoD Contract Fund Reconciliation Process, December 5, 1997. Contract fund reconciliation is the process of matching obligation and disbursement data in contracting, disbursing, and accounting and finance systems to the specifications in the contract document. All DoD contracts eventually require contract fund reconciliation. Many contracts require reconciliation only at contract close-out. However, the large and complicated contracts for major weapon systems are frequently out of balance during their life cycle and require immediate reconciliation. During FY 1996, the DFAS Columbus Center and the Military Departments identified 9,652 contracts that were out of balance by a total of more than $1 billion. The audit found inefficient processes that were unnecessarily costly, time consuming, and ineffective in terms of facilitating accurate reporting, prompt payment and timely contract close-out.

Specifically, the Military Departments and DFAS did not routinely distribute the results of contract reconciliations, so much of the work was wasted. The inability to keep contracts in balance contributed to the Military Departments' need to obligate current-year funds to cover unmatched disbursements and negative unliquidated obligations that were more than 180 days old.

The DoD organizations did not use standardized methods to perform contract reconciliation. Also, automated reconciliation systems in use and under development lacked a standardized output. As a result, contract fund reconciliations were not readily accepted or exchanged by the various DoD Components that performed them, resulting in duplication of reconciliation efforts. In FY 1996, 278 contracts were reconciled concurrently. Last, DFAS Columbus Center did not ensure that Defense agencies with Army Fiscal Station numbers received copies of internal adjustments. As a result, contracts at those Defense agencies required extensive reconciliations.

Report No. 98-002, A Status Report on the Major Accounting and Management Control Deficiencies in the Defense Business Operations Fund for FY 1996, October 3, 1997. The FY 1996 Defense Business Operations Fund financial statements identified assets of $92.2 billion, liabilities of $18.4 billion, and revenues of $73.7 billion.

We identified significant accounting and management control deficiencies in the Defense Business Operations Fund that prevented the timely development and reliable presentation of the financial statements. The deficiencies were:

- Interim Migratory Accounting Strategy;
- cash management;
- standard general ledger;

- documentation and audit trails;
- property, plant, and equipment;
- valuation and reporting of inventory; and
- personnel.

The problems that were identified affected approximately 67.8 percent of total assets and 16.6 percent of total revenues. The deficiencies resulted in auditor recommended adjustments of $75.1 billion to the FY 1996 financial statements and the supporting accounting records. Many of the deficiencies noted in last year's report remain uncorrected, as candidly acknowledged by the Under Secretary of Defense (Comptroller) in his Management Representation Letter.

# FY 1997 CFO Audit Opinions

| Report Title | Audit Organization | Opinion |
|---|---|---|
| Disclaimer of Opinion on the Department of Defense Consolidated Financial Statements for FY 1997 | OIG, DoD | Disclaimer |
| Army's Principal Financial Statements for Fiscal Years 1997 and 1996 | Army Audit Agency | Disclaimer |
| Army Working Capital Fund Principal Financial Statements for FY 1997 | Army Audit Agency | Disclaimer |
| FY 97 Financial Statements Opinion Report U.S. Army Corps of Engineers, Civil Works[1] | Army Audit Agency | Disclaimer |
| Department of the Navy Principal Statements for Fiscal Years 1997 and 1996: Report on Auditor's Opinion | Naval Audit Service | Disclaimer |
| Independent Auditor's Opinion on the Statement of Financial Position of the FY 1997 Department of the Navy Working Capital Fund Consolidated Financial Statements | Naval Audit Service | Disclaimer |
| Report of Audit, Opinion on Fiscal Year 1997 Air Force Consolidated Financial Statements | Air Force Audit Agency | Disclaimer |
| Report of Audit, Opinion on Fiscal Year 1997 Air Force Working Capital Fund Financial Statements | Air Force Audit Agency | Disclaimer |
| Audit Opinion on the Defense Logistics Agency Working Capital Fund Financial Statements for FY 1997 | OIG, DoD | Disclaimer |
| Disclaimer of Opinion on the Defense Information Systems Agency Defense-Wide Working Capital Fund Financial Statements for FY 1997 | OIG, DoD | Disclaimer |
| Disclaimer of Opinion on the Defense Finance and Accounting Service Working Capital Fund Financial Statements for FY 1997 | OIG, DoD | Disclaimer |

[1] Southwest Division statements received an unqualified opinion.

| | | |
|---|---|---|
| Disclaimer of Opinion on the Defense Commissary Agency Financial Statements for FY 1997 | OIG, DoD | Disclaimer |
| Audit Opinion on the Military Retirement Trust Fund Financial Statements for FYs 1997 and 1996 | OIG, DoD | In Process |
| Disclaimer of Opinion on the National Defense Stockpile Transaction Fund Financial Statements for FY 1997 | OIG, DoD | Disclaimer |
| Disclaimer of Opinion on the Defense Security Assistance Agency Financial Statements for FY 1997 | OIG, DoD | Disclaimer |
| Disclaimer of Opinion on the Joint Logistics Systems Center Working Capital Fund Financial Statements for FY 1997 | OIG, DoD | Disclaimer |