Audit Report

COMPILATION OF DEFENSE LOGISTICS AGENCY
CASH TRANSACTIONS

Report No. 00-011 October 18, 1999

Office of the Inspector General
Department of Defense

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Acronyms

ACRS	Appropriation Control and Reporting System
DAPS	Defense Automated Printing Service
DBOF	Defense Business Operations Fund
DFAS	Defense Finance and Accounting Service
DLA	Defense Logistics Agency
HQARS	Headquarters Accounting and Reporting System

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2884

October 18, 1999

MEMORANDUM FOR DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE

SUBJECT: Audit Report on Compilation of Defense Logistics Agency Cash Transactions (Report No. 00-011)

We are providing this report for your information and use. We considered management comments on a draft of this report in preparing the final report.

Comments to the recommendations in the draft of this report conformed to the requirements of DoD Directive 7650.3 and no further comments are required.

We appreciate the courtesies extended to the audit staff. Questions about the audit should be directed to Mr. James L. Kornides at (614) 751-1400, extension 11, (jkornides@dodig.osd.mil) or Mr. Stuart D. Dunnett at (614) 751-1400, extension 14 (sdunnett@dodig.osd.mil). See Appendix B for the report distribution. The audit team members are listed inside the back cover.

Robert J. Lieberman
Assistant Inspector General
For Auditing

Office of the Inspector General, DoD

Report No. 00-011 **October 18, 1999**
(Project No. 8FJ-2013.01)

Compilation of Defense Logistics Agency Cash Transactions

Executive Summary

Introduction. This is the second in a series of reports on the compilation of the Defense agencies' FY 1998 financial statements at the Defense Finance and Accounting Service (DFAS) Columbus Center, Columbus, Ohio. The DFAS Columbus Center compiles the financial statements of the Defense Logistics Agency, DFAS, the Defense Commissary Agency, and the Defense Contract Audit Agency. The Defense Logistics Agency is the cash manager of the Defense-Wide Working Capital Fund, which includes DFAS, the Defense Information Systems Agency, the Joint Logistics Support Command, and five Defense Logistics Agency activity groups.

Cash transactions consist of collections and disbursements that are reported to the U.S. Treasury through the DoD finance network and later posted to the general ledger accounts by the DFAS Centers and operating locations. The DFAS Indianapolis Center, Indianapolis, Indiana, consolidates cash transactions for the Defense-Wide Working Capital Fund and reports the consolidated information to the U.S. Treasury. Any differences between the amounts reported to the U.S. Treasury and the amounts posted to general ledger accounts need to be reconciled to ensure the accuracy and reliability of financial data. In FY 1998, cash transactions that were compiled in the Defense Logistics Agency's financial statements totaled $28.6 billion.

Objectives. The overall objective of the audit was to determine whether the DFAS Columbus Center consistently and accurately compiled financial data from field organizations and other sources for the Defense agency financial statements for which the DFAS Columbus Center was responsible. This part of the audit focused on whether the DFAS Columbus and Indianapolis Centers adequately reconciled the Defense Logistics Agency's cumulative collections and disbursements to amounts reported to the U.S. Treasury by the former Defense Accounting Office, Arlington, Virginia, and the DFAS Indianapolis Center.

Results. The DFAS Columbus Center did not reconcile $688.3 million in Defense Logistics Agency collections and $1,174.6 million in Defense Logistics Agency disbursements to the amounts reported to the U.S. Treasury for FYs 1992 through 1998. In addition, the DFAS Cleveland Center and DFAS Operating Location Charleston, Charleston, South Carolina, did not reconcile $445.4 million in unmatched cash transactions that were reported to the U.S. Treasury for FYs 1997 and 1998. The unreconciled transactions were reported on the Defense Logistics Agency's financial statements as unsupported upward and downward adjustments to accounts payable and

accounts receivable. The DFAS Columbus Center began correcting the cash reconciliation problems, but did not complete all required actions. As a result, the DFAS Columbus Center made the following unsupported net adjustments to the FY 1998 Defense Logistics Agency Consolidated Balance Sheet: $898.4 million to accounts payable and $166.7 million to accounts receivable. In addition, the unreconciled cash transactions had an undeterminable effect on the Defense Logistics Agency's obligated balances and the Fund Balance With Treasury account. Unless those conditions are corrected, the Defense Logistics Agency's financial statements for FY 1999 and later will not be compiled accurately or consistently.

See Appendix A for details of the review of the management control program.

Summary of Recommendations. We recommend that the Director, Defense Finance and Accounting Service, expedite the identification of undistributed Defense Logistics Agency collections and disbursements by the DFAS Columbus and Indianapolis Centers; identify and correct underreported collections and disbursements for the Defense Logistics Agency Distribution Depot activity group; and establish procedures for correcting the financial data reported for the Defense Automated Printing Service.

Management Comments. The Director for Accounting, DFAS, concurred with the recommendations and indicated that reconciliation procedures on undistributed amounts would be completed by June 30, 2000. A complete text of management comments is in the Management Comments section.

Audit Response. The Director for Accounting, DFAS, comments to the recommendations were responsive. No further response is required.

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Background

The Defense Finance and Accounting Service (DFAS) Columbus Center, Columbus, Ohio, compiles the financial statements of the Defense Logistics Agency, DFAS, the Defense Commissary Agency, and the Defense Contract Audit Agency. Compilation is the preparation of financial statements from summary accounting information provided by financial and logistics feeder systems. The DFAS Columbus Center prepares the information in the format defined by the Office of Management and Budget and implemented in DoD through guidance issued by the Under Secretary of Defense (Comptroller).

This is the second in a series of reports on the compilation of the Defense agencies' FY 1998 financial statements at the DFAS Columbus Center. The first report discussed the compilation of Defense Reutilization and Marketing Service operating results. This report discusses the compilation of DLA cash transactions by the DFAS Columbus Center.

The DFAS Columbus Center provides accounting support and compilation for four DLA activity groups: Supply Management, Distribution Depot, the Defense Reutilization and Marketing Service, and Information Services. The DFAS Operating Location Charleston, Charleston, South Carolina, and the DFAS Cleveland Center, Cleveland, Ohio, provided accounting support for the Defense Automated Printing Service in FY 1998. The DFAS Columbus Center compiled the consolidated FY 1998 DLA financial statements and was to compile the financial statements for all activity groups in FY 1999.

DLA is also the cash manager for the Defense-Wide Working Capital Fund, which includes DLA, DFAS, and the Defense Information Systems Agency. Cash transactions (collections and disbursements) are reported to the U.S. Treasury through the DoD finance network and are later posted to general ledger accounts by the DFAS Centers and operating locations. The DFAS Indianapolis Center consolidates cash transactions for the Defense-Wide Working Capital Fund and reports the consolidated information to the U.S. Treasury. Differences between the amounts reported to the U.S. Treasury and the amounts posted to general ledger accounts need to be reconciled to ensure the accuracy and reliability of financial data. In FY 1998, cash transactions that were compiled in the DLA financial statements totaled $28.6 billion.

Undistributed collections and disbursements are cash transactions that have not been reconciled; these transactions affect the completeness, accuracy, and reliability of DoD account balances. Collections and disbursements can be unreconciled for many reasons, including timing differences, poor recordkeeping, inadequate documentation, inadequate systems, and lack of resources. The FY 1998 DLA financial statements reported more than $1 billion of unreconciled cash transactions.

Objectives

The overall objective of the audit was to determine whether the DFAS Columbus Center consistently and accurately compiled financial data from field organizations and other sources for the Defense agency financial statements for which the DFAS Columbus Center was responsible. This part of the audit focused on whether the DFAS Columbus Center and the DFAS Indianapolis Center, Indianapolis, Indiana, adequately reconciled DLA cumulative collections and disbursements to amounts reported to the U.S. Treasury by the former Defense Accounting Office, Arlington, Virginia, and the DFAS Indianapolis Center.

Compilation of Defense Logistics Agency Collections and Disbursements

When compiling DLA cash transactions, the DFAS Columbus Center did not reconcile $688.3 million in DLA collections and $1,174.6 million in DLA disbursements to the amounts reported to the U.S. Treasury for FYs 1992 through 1998. In addition, the DFAS Cleveland Center and DFAS Operating Location Charleston did not reconcile $445.4 million in unmatched cash transactions. The DFAS Columbus Center compiled unreconciled transactions on the DLA financial statements as unsupported upward and downward adjustments to accounts payable, accounts receivable, obligated balances, and other liabilities. The DFAS Centers did not reconcile the transactions because the DFAS systems used to compile and report summary data to the U.S. Treasury did not maintain adequate records of the supporting cash transactions, and the DFAS Indianapolis Center did not establish procedures to identify and correct undistributed collections and disbursements from prior years. The DFAS Columbus Center began correcting the cash reconciliation problems, but actions were not completed. As a result, the DFAS Columbus Center made the following unsupported net adjustments to the FY 1998 DLA Consolidated Balance Sheet: $898.4 million to accounts payable and $166.7 million to accounts receivable. In addition, the unreconciled cash transactions had an undeterminable effect on DLA obligated balances and the Fund Balance With Treasury account. Unless those conditions are corrected, the DLA financial statements for FY 1999 and later will not be compiled accurately or consistently.

Accounting Guidance

DoD Regulation 7000.14-R, the "DoD Financial Management Regulation," volume 6B, "Form and Content of the Department of Defense Audited Financial Statements," December 1998, provides DoD guidance on the compilation of DoD financial statements. Primary responsibility for the content and submission of the audited financial statements rests with the head of the reporting entity for which the statements are prepared. The actual preparation of the financial statements is the joint responsibility of DFAS and the DoD reporting entity.

DoD Regulation 7000.14-R, volume 5, "Disbursing Policy and Procedures," August 1998, provides DoD guidance on reporting cash transactions to the U.S. Treasury. The regulation requires cash transactions to be balanced daily. After the cash transactions are reported to the U.S. Treasury, the DFAS Centers and operating locations post the cash transactions to DoD accounts in accordance with DoD Regulation 7000.14-R, volume 4, "Accounting Policy and Procedures," January 1995. Volume 4 requires the cash amounts reported to the U.S. Treasury to be reconciled with the cash amounts posted to DoD

accounting systems and requires the correction of discrepancies. Volume 4 also requires accounts payable and accounts receivable to be reconciled to supporting documentation at least annually.

DoD Regulation 7000.14-R, volume 3, "Budget Execution - Availability and Use of Budgetary Resources," December 1996, prescribes accounting standards and management requirements to establish and maintain financial control over disbursement, collection, and adjustment transactions affecting the Fund Balance With Treasury account and other cash resources. Volume 3 requires the DoD Components to obligate funds for overaged, unmatched, and negative unliquidated obligations and provides specific procedures for researching and resolving problem disbursements. Overaged disbursements are defined as in-transit disbursements that are more than 180 days in age.

Chronology of Reporting to U.S. Treasury

Since the implementation of the Chief Financial Officers Act of 1990, which required DoD to produce financial statements beginning in 1991, DLA and DFAS have had problems reconciling collection and disbursement information. From FY 1992 through the first quarter of FY 1995, the former Defense Accounting Office, Arlington, Virginia, used the Appropriation Control and Reporting System (ACRS) to report collections and disbursements to the U.S. Treasury for the former Defense Business Operations Fund (DBOF), which included DLA. The ACRS compiled DBOF cash transactions into one account and reported the compiled data to the U.S. Treasury. The Under Secretary of Defense (Comptroller) was responsible for managing the single cash account for all DBOF business areas.

The ACRS also compiled DBOF data into cash reports that summarized cash transactions by DBOF business area and were distributed to the DFAS Centers, DFAS operating locations, and users in the DBOF business areas. The amounts on the cash reports were compiled into SF 133, "Report on Budget Execution," for each business area.

In January 1995, the Under Secretary of Defense (Comptroller) changed the cash management policy for DBOF and made the Military Departments and DLA responsible for managing cash. As a result, in March 1995, the Defense Accounting Office was no longer responsible for reporting to the U.S. Treasury and no longer used ACRS. The DFAS Indianapolis, Denver, and Cleveland Centers became responsible for reporting cash amounts to the U.S. Treasury.

Instead of ACRS, the DFAS Indianapolis Center used the Headquarters Accounting and Reporting System (HQARS) to report Army and DLA cash amounts (except for the Defense Automated Printing Service [DAPS] activity group) to the U.S. Treasury. HQARS consists of 10 subsystems that compile collections and disbursements from the Military Departments, Defense agencies, the Department of State, and other Government entities. The DFAS Cleveland Center reported cash transactions for the DAPS activity group.

HQARS also produces cash reports that are distributed to DLA and other users. The amounts reported on the cash reports are compiled into SF 133 for each business area. DLA also uses the reports to manage the cash accounts for the Defense-Wide Working Capital Fund. The HQARS system was scheduled to be replaced by the Corps of Engineers Financial Management System in December 1998, but the replacement has been postponed indefinitely. As of May 1999, cash reporting functions for the Army and Defense agencies were being converted to the Defense Cash Accountability System.

DFAS Columbus Center's Reconciliation Efforts

The DFAS Columbus Center did not reconcile $688.3 million in DLA collections and $1,174.6 million in DLA disbursements to the amounts reported to the U.S. Treasury for FYs 1992 through 1998 by the DFAS Indianapolis and Cleveland Centers and the former Defense Accounting Office, Arlington, Virginia. The DFAS Columbus Center did not reconcile the cash transactions because the DFAS systems used to compile and report summary data to the U.S. Treasury did not maintain adequate records of the supporting cash transactions, and the DFAS Indianapolis Center did not establish procedures to identify and correct undistributed collections and disbursements from prior years. The DFAS Columbus Center began correcting the cash reconciliation problems, but actions were not completed.

Reporting to U.S. Treasury, FYs 1992 Through 1995. The DFAS Indianapolis Center could not locate ACRS reports for FYs 1992 and 1995, and ACRS reports for FYs 1993 and 1994 did not identify the number and amounts of DLA undistributed collections and disbursements that were reported to the U.S. Treasury. Instead, undistributed collections and disbursements for DLA and other Defense agencies were combined and reported to the U.S. Treasury along with Army transactions. As a result, DLA collections and disbursements were distorted.

For example, the reporting of cash transactions for the DLA Distribution Depot activity showed that collections and disbursements for cash listings were significantly less than collections and disbursements posted to DLA accounting records from FYs 1992 through 1998 (see Tables 1 and 2).

Table 1. Cumulative Distribution Depot Collections

Fiscal Year	Cash Listings	Trial Balance	Undistributed
1992	$ 95,063,357	$ 95,481,217	$ 417,860
1993	1,495,176,844	1,375,856,799	(119,320,045)
1994	1,330,429,117	1,753,287,372	422,858,255
1995	1,266,313,073	1,326,144,461	59,831,388
1996	1,708,003,496	1,559,934,651	(148,068,845)
1997	1,279,364,415	1,279,642,482	278,067
1998	1,266,791,086	1,265,027,240	(1,763,846)
Total	**$8,441,141,388**	**$8,655,374,222**	**$214,232,834**

Table 2. Cumulative Distribution Depot Disbursements

Fiscal Year	Cash Listings	Trial Balance	Undistributed
1992	$ 862,039,633	$ 737,431,480	$ (124,608,153)
1993	1,148,341,506	1,414,357,819	266,016,313
1994	1,563,204,328	1,519,226,339	(43,977,989)
1995	1,594,191,875	1,528,481,015	(65,710,860)
1996	1,715,448,165	1,639,109,054	(76,339,111)
1997	1,567,967,443	1,603,833,695	35,866,252
1998	1,451,265,487	1,535,456,036	84,190,549
Total	**$9,902,458,437**	**$9,977,895,438**	**$ 75,437,001**

The cumulative cash listings for collections and disbursements should be larger than the cumulative trial balance listings because cash transactions are first made by disbursing stations and later posted to the accounting records that support the trial balance. The undistributed cash transactions should be identified on problem disbursement reports. However, the DFAS Columbus Center's problem disbursement reports did not identify $214.2 million in undistributed collections and $75.4 million in undistributed disbursements.

The undistributed collections and disbursements for the Distribution Depot were caused by errors in the trial balances or underreporting of the transactions on the

cash listings. The DFAS Columbus and Indianapolis Centers should identify and correct the errors; or, if the cash transaction collections were underreported, as indicated by ACRS reporting problems, the DLA Fund Balance With Treasury account should be increased by $138.8 million ($214.2 million in underreported collections minus $75.4 million in underreported disbursements). In either case, the cash transactions for the Distribution Depot distorted the amounts shown on the DLA financial statements because the DFAS Columbus Center adjusted the DLA accounts receivable for the undistributed collections and DLA accounts payable for the undistributed disbursements.

HQARS Reporting Since March 1995. Cash managers stated that in March 1995, the U.S. Treasury reporting functions for Army and Defense agency cash transactions were transferred to the DFAS Indianapolis Center. However, the DFAS Indianapolis Center did not issue procedures to identify or clear undistributed cash transactions that were reported by ACRS from FYs 1992 through 1995. In addition, the HQARS system did not give the DFAS Columbus Center adequate visibility over cash transactions reported to the U.S. Treasury from March 1995 through February 1999. As a result, the DFAS Columbus Center could not reconcile DLA cash accounts.

In May 1998, the Director of Accounting at the DFAS Columbus Center established a Cash Reconciliation Task Group to determine the most effective methods of reconciling undistributed Defense agency cash transactions to the official accounting records. The task group found that the DFAS Indianapolis Center was not providing the DFAS Columbus Center with visibility over collections and disbursements that the HQARS system reported to the U.S. Treasury.

The HQARS weaknesses are long-standing. We reported the lack of audit trails to DLA cash amounts reported to the U.S. Treasury in IG, DoD, Report No. 94-159, "Fund Balance With Treasury Accounts of the FY 1993 Financial Statements of the DLA Business Areas of the Defense Business Operations Fund," June 30, 1994. DoD management agreed to correct the systemic weaknesses identified in the audit report, but the DFAS Indianapolis Center did not issue procedures to identify undistributed cash transactions.

In October 1998, the DFAS Columbus and Indianapolis Centers signed a memorandum of agreement to correct problems with reporting to the U.S. Treasury. The memorandum identified 11 actions that the DFAS Indianapolis Center agreed to complete by November 1, 1998.

The 11 actions were designed to provide audit trails to Defense agency transactions that HQARS reported to the U.S. Treasury. The DFAS Indianapolis Center was to change treasury routing codes, accounting limit codes, and pseudo codes (all used by the HQARS system). In addition, the DFAS Indianapolis Center agreed to issue guidance on fiscal station numbers and provide the DFAS Columbus Center with electronic files of all transactions. The DFAS Indianapolis Center agreed to complete the actions by

November 1, 1998. A followup report issued by the DFAS Columbus Center on February 23, 1999, stated that the DFAS Indianapolis Center had not completed work on any of the 11 actions.

On March 3, 1999, we met with the Director, DFAS Columbus Center, to determine what should be done to correct the problems with reporting to the U.S. Treasury. After the meeting, DFAS Columbus Center personnel did more work on the 11 required actions. The DFAS Columbus Center reported improvement, but did not complete the actions because cash reporting functions for the Army and Defense agencies were being converted to the Defense Cash Accountability System.

At a meeting at the DFAS Columbus Center in May 1999, we learned that the 11 actions had not been completed. The meeting included representatives from DFAS headquarters and the DFAS Centers. The DFAS Columbus and Indianapolis Centers had not developed an adequate plan for identifying undistributed DLA collections and disbursements. The Director, DFAS, should expedite the identification of undistributed DLA collections and DLA disbursements by DFAS Columbus and Indianapolis Centers.

Reconciliation of Defense Automated Printing Service Collections and Disbursements

The Operating Location Charleston could not reconcile cash balances for the Defense Automated Printing Service (DAPS) activity group during FYs 1997 and 1998. Cash balances were unreconcilable because the Defense Working Capital Fund Accounting System did not properly process collections and disbursements during FYs 1997 and 1998. As a result, the DFAS Cleveland Center made unsupported adjustments to DAPS obligations and the Fund Balance With Treasury account, which the DFAS Columbus Center consolidated into the FY 1998 DLA financial statements.

Selection of the Defense Working Capital Fund Accounting System. In FY 1997, DFAS fielded the Defense Working Capital Fund Accounting System as a commercial off-the-shelf system to replace the existing DAPS accounting system. The evaluation, testing, and fielding of the Defense Working Capital Fund Accounting System were inadequate; as a result, the Defense Working Capital Fund Accounting System inappropriately processed $445.4 million in collections and disbursements into a suspense account. The $445.4 million had indeterminable effects on other accounts, including FY 1998 obligated balances. We also identified a $106.2 million unsupported net adjustment to the DAPS Fund Balance With Treasury account. DLA questioned the unreliable financial information in the DAPS accounts in Note 16, which stated the following:

> Because of financial information system problems and financial statement compilation problems, DLA believes that the Defense Automated Printing Service (DAPS) financial statements are not completely representative of the DAPS financial position. DLA

management does not believe that this will materially affect the fiscal year 1998 DLA Working Capital Fund Chief Financial Officers Annual Financial Statement. At September 30, 1998, DAPS assets represented less than 1 percent of the total DLA combined assets, DAPS revenues represented approximately 2.4 percent of total DLA combined revenues and DAPS expenses represented approximately 2.6 percent of total DLA combined expenses.

The footnote disclosure was incomplete because it did not mention the $445.4 million in collections and disbursements that were processed into a suspense account. DFAS headquarters did not validate the budgetary functions of the Defense Working Capital Fund Accounting System before it was fielded, and we could not determine how the $445.4 million affected the DLA obligated balances. However, the $445.4 million represented almost 10 percent of the FY 1998 DLA consolidated balance of $4.6 billion.

The Director, DFAS, needs to establish procedures for correcting financial data reported for the DAPS in coordination with the DLA Comptroller. The procedures should ensure that FY 1998 reporting problems are adequately disclosed on the FY 1999 DLA financial statements. Issues regarding the acquisition, evaluation, testing, and fielding of commercial off-the-shelf financial systems will be addressed in a separate audit report.

Consolidated Effects of Undistributed Cash Transactions

The undistributed cash transactions have direct and material effects on the FY 1998 DLA financial statements. The DFAS Columbus Center compiled $688.3 million in DLA undistributed collections as downward and upward adjustments to accounts receivable for DLA activity groups. The DFAS Columbus Center also compiled $1,174.6 million in undistributed disbursements as downward and upward adjustments to accounts payable.

The downward and upward adjustments resulted in the following net adjustments to the FY 1998 DLA Consolidated Balance Sheet: $898.4 million to accounts payable and $166.7 million to accounts receivable.

The unreconciled cash transactions also had an undeterminable effect on DLA obligated balances and the Fund Balance With Treasury accounts. Unless those conditions are corrected, the DLA financial statements for FY 1999 and later will not be compiled accurately or consistently.

Recommendations and Management Comments

We recommend that the Director, Defense Finance and Accounting Service:

1. Expedite the identification of undistributed Defense Logistics Agency collections and disbursements by the Defense Finance and Accounting Service Columbus and Indianapolis Centers.

Management Comments. The Director for Accounting, DFAS, concurred and stated that each DFAS Center is in the process of validating it's cash reconciliation process, defining undistributed transactions, and ascertaining the dollar value of current and prior year undistributed balances. DFAS stated that it's goal is to stabilize undistributed dollars, ascertain balances, and work with the Office of the Under Secretary of Defense (Comptroller) to determine appropriate corrective action.

2. Identify and correct underreported collections and disbursements for the Defense Logistics Agency Distribution Depot activity group.

Management Comments. The Director for Accounting, DFAS, concurred and stated that they will identify and correct underreported transactions as part of their corrective action.

3. Establish procedures for correcting financial data reported for the Defense Automated Printing Service, in coordination with the Defense Logistics Agency Comptroller. The procedures should require the Defense Finance and Accounting Service Columbus Center and the Defense Logistics Agency Comptroller to adequately disclose FY 1998 reporting problems on the FY 1999 Defense Logistics Agency financial statements.

Management Comments. The Director for Accounting, DFAS, concurred and stated that the DFAS Columbus Center will work with DLA to establish procedures for correcting Defense Automated Printing Service financial data and make proper disclosures in the FY 1999 CFO Financial Statements.

Appendix A. Audit Process

Scope

Work Performed. We evaluated DLA collection and disbursement records to determine whether the DFAS Columbus Center could reconcile DLA cumulative collections and disbursements to amounts reported to the U.S. Treasury by the DFAS Indianapolis Center and the former Defense Accounting Office, Arlington, Virginia, from FYs 1992 through 1998. We also completed trend analyses on cumulative DLA balances of collections and disbursements from FYs 1992 through 1998. In total, we analyzed summary records related to $93.7 billion in collections and $89.1 billion of disbursements reported for the following DLA activity groups: Supply Management, Distribution Depot, and the Defense Reutilization and Marketing Service. We also completed analyses of FY 1997 and 1998 collections and disbursements reported for the DAPS and Information Services activity groups.

We determined whether the DFAS systems used to compile and report summary data to the U.S. Treasury maintained adequate records of the supporting cash transactions, and whether the DFAS Indianapolis Center established procedures to identify and correct undistributed collections and disbursements from prior years. We also determined the effect of unreconciled cash transactions on DLA financial statements. Specifically, we determined the gross and net effects of unreconciled cash transactions on DLA accounts payable, accounts receivable, other liabilities, and obligated balances.

Use of Computer-Processed Data. We relied on computer-processed data to form our conclusions. We analyzed summary accounting records provided by the DFAS Columbus and Indianapolis Centers for DLA collections and disbursements from FYs 1992 through 1998. We analyzed the data to determine whether undistributed collections and disbursements from prior years were distributed by the DFAS Indianapolis Center. We did not perform tests to determine the accuracy of the computer-processed data. We did not use statistical sampling methods.

DoD-Wide Corporate-Level Government Performance and Results Act Goals. In response to the Government Performance and Results Act, DoD established 6 DoD-wide corporate-level performance objectives and 14 goals for meeting those objectives. Project No. 8FJ-2013.01 pertains to the achievement of the following objective and goal.

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

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

- **Financial Management Functional Area**
  Objective: Consolidate finance and accounting operations.
  Goal: Reduce and improve accounting systems. **(FM-2.2)**

- **Financial Management Functional Area**
  Objective: Eliminate problem disbursements.
  Goal: Improve the processing and control over cross-disbursements. **(FM-3.2)**

- **Financial Management Functional Area**
  Objective: Eliminate problem disbursements.
  Goal: Improve timeliness and accuracy of obligations. **(FM-3.3)**

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

General Accounting Office High-Risk Area. The General Accounting Office had identified several high-risk areas in DoD. This report provides coverage of the financial management high-risk area.

Audit Type, Dates, and Standards. We performed this financial-related audit from August 1998 through August 1999 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. We included tests of management controls considered necessary.

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

Management Control Program

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

Scope of Review of the Management Control Program. DFAS identified the reconciliation of undistributed and unmatched cross-disbursing and interfund cash transactions as an unresolved material management control weakness on the DFAS FY 1997 and FY 1998 Annual Statement of Assurance. Our audit provided assistance to DFAS in identifying the causes of the material

management control weakness. The causes identified in this report were not reported as material weaknesses by the DFAS Columbus or Indianapolis Centers. The review of the management control program as it related to the overall objective will be discussed as part of a later report.

Adequacy of Management Controls. We identified a material management control weakness for DFAS, as defined in DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996. DFAS management controls were not adequate to ensure that the collections and disbursements were properly distributed to DLA activity groups. The recommendations, if implemented, will allow DFAS to correct long-standing problems in the reconciliation of DLA cash accounts. A copy of the report will be provided to the senior official in charge of the DFAS management control program.

Adequacy of Management's Self-Evaluation. Management's self-evaluation was inadequate. The DFAS Columbus and Indianapolis Centers did not report the material weaknesses identified in this report because assessable units were not specific enough to identify the causes of undistributed cash transactions. The Director for Accounting, DFAS, disagreed with the auditors' assertions that management's self-evaluation of controls was inadequate and indicated that undistributed and unmatched material weaknesses were reported in the DFAS Statement of Assurance. We disagree with the Director's comments regarding the adequacy of management's self-evaluation of controls. Although undistributed and unmatched material weaknesses were reported in the DFAS Statement of Assurance at the corporate level, DFAS Columbus Center and DFAS Indianapolis Center must report the material weaknesses related to DLA undistributed collections and disbursements in their Statements of Assurance until their control weaknesses are corrected.

Summary of Prior Coverage

The Inspector General, DoD, has issued one report with related audit coverage: Report No. 94-159, "Fund Balance With Treasury Accounts of the FY 1993 Financial Statements of the Defense Logistics Agency Business Areas of the Defense Business Operations Fund," June 30, 1994.

Appendix B. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Comptroller)
  Deputy Chief Financial Officer
  Deputy Comptroller (Program/Budget)
Director, Defense Logistics Studies Information Exchange

Department of the Army

Auditor General, Department of the Army

Department of the Navy

Assistant Secretary of the Navy (Financial Management and Comptroller)
Auditor General, Department of the Navy

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and Comptroller)
Auditor General, Department of the Air Force

Other Defense Organizations

Director, Defense Finance and Accounting Service
Director, Defense Contract Audit Agency
Director, Defense Logistics Agency
Director, National Security Agency
  Inspector General, National Security Agency
Inspector General, Defense Intelligence Agency

Non-Defense Federal Organizations

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

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

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

Defense Finance and Accounting Service Comments

DEFENSE FINANCE AND ACCOUNTING SERVICE
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DFAS-HQ/ASF

SEP 27 1999

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

SUBJECT: Audit Report on the Compilation of Defense Logistics Agency Cash Transactions (Project No 8FJ-2013.01)

Our response to the subject audit is attached The primary point of contact (POC) is Mr Wayne Ebaugh, (703) 607-2857 or DSN 327-2857, and the secondary POC is Mr Mike Bryant, (703) 607-1562 or DSN 327-1562.

for Edward A Harris
Director for Accounting

Attachment:
As stated

cc
DFAS-HQ/PO
DFAS-IN/PII
DFAS-CO/A
DFAS-CO/DI

DFAS Comments on Department of Defense Inspector General Draft Report "Compilation of Defense Logistics Agency Cash Transactions" (Project No. 8FJ-2013.01)

Responses to Recommendations

We recommend that the Director, Defense Finance and Accounting Service:

Recommendation 1. Expedite the identification of undistributed Defense Logistics Agency collections and disbursements by the Defense Finance and Accounting Service Columbus and Indianapolis Centers.

DFAS Management Comments: Concur. The DFAS is validating each Center's cash reconciliation processes, defining undistributed collections and disbursements, and ascertaining the dollar values of supportable and unsupportable current and prior years undistributed balances at a detail transaction level. The DFAS Indianapolis Center (DFAS-IN) is clearing the Unreconciled Input Data Report for all transactions processed prior to November 1998, resolving file maintenance issues, and correcting the use of pseudo disbursing station symbol numbers in the Uncleared File. The DFAS-IN is also reconciling Treasury balances for Treasury Index 97 Funds. The DFAS Columbus Center (DFAS-CO) is currently performing cash reconciliations on a monthly basis for all appropriations and funds for which it is producing agency-level reports. The DFAS-CO can support the FY 1999 undistributed dollars at the detail transaction level.

Under our current reconciliation procedures, our goal is to stabilize the unsupported undistributed dollars. Once the unsupported undistributed dollars are stabilized and the balances are ascertained, the DFAS will work with the OUSD(C) to determine appropriate corrective action.

Estimated Completion Date: June 30, 2000

Recommendation 2. Identify and correct underreported collections and disbursements for the Defense Logistics Agency distribution depot activity group.

DFAS Management Comments: Concur. The DFAS will identify and correct under-reported collections and disbursements as part of the corrective action that the DFAS will take in response to Recommendation 1.

Estimated Completion Date: June 30, 2000

Recommendation 3. Establish procedures for correcting financial data reported for the Defense Automated Printing Service in coordination with the Defense Logistics Agency Comptroller. The procedures should require the Defense Finance and Accounting Service Columbus Center and the Defense Logistics Agency, Comptroller, to adequately disclose FY 1998 reporting problems on the FY 1999 Defense Logistics Agency financial statements.

DFAS Management Comments: Concur. The DFAS Columbus Center will work with the Defense Logistics Agency to establish procedures for correcting financial data and make

proper disclosure of FY 1998 reporting problems for the Defense Automated Printing Service in the footnotes to Version "1" of the FY 1999 CFO Financial Statements

Estimated Completion Date: June 30, 2000

Management Control Program Comments

The DFAS disagrees with the auditor's assertion that management's self-evaluation was inadequate and that the material weaknesses were not reported because assessable units were too large. As referenced in the audit, the DFAS reported an undistributed and unmatched material weakness in its FY 1997 and FY 1998 Annual Statement of Assurance. The conditions noted in the audit are covered by that weakness and do not warrant separate reporting.

Audit Team Members

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

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