Audit Report

OFFICE OF THE INSPECTOR GENERAL

DEFENSE LOGISTICS AGENCY
GENERAL FUND EQUIPMENT ACCOUNT

Report No. 97-039

December 5, 1996

Department of Defense

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Acronyms

DCMD	Defense Contract Management District
DBMS	Defense Business Management System
DBOF	Defense Business Operations Fund
DFAS	Defense Finance and Accounting Service
DLA	Defense Logistics Agency

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December 5, 1996

MEMORANDUM FOR DIRECTOR, DEFENSE LOGISTICS AGENCY
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE

SUBJECT: Audit Report on the Defense Logistics Agency General Fund Equipment Account (Report No 97-039)

We are providing this audit report for your review and comment. Management comments on a draft of this report were considered in preparing the final report. This report discusses the Defense Logistics Agency General Fund Equipment account and is one in a series of reports on our assessment of the internal controls and the compliance of the Defense Logistics Agency and the Defense Finance and Accounting Service with laws and regulations relating to financial management at the Defense Logistics Agency (Project No. 6LA-2005). We have issued a final report on the general fund trial balance, and a draft report on the preparation of the general fund financial statements.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The Defense Logistics Agency concurred with Recommendation B.2., but did not state the action to be taken. Therefore, we ask the Defense Logistics Agency to provide additional comments by February 3, 1997.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Robert J. Ryan, Audit Program Director, at (703) 604-9418 (DSN 664-9418), or Mr. Garry A. Hopper, Audit Project Manager, at (703) 604-9612 (DSN 664-9612). See Appendix E for the report distribution. The audit team members are listed on the inside back cover.

David K. Steensma

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Office of the Inspector General, DoD

Report No. 97-039
(Project No. 6LA-2005.02)

December 5, 1996

Defense Logistics Agency
General Fund Equipment Account

Executive Summary

Introduction. This report is one in a series of reports on our assessment of the internal controls and the compliance of the Defense Logistics Agency (DLA) and the Defense Finance and Accounting Service (DFAS) with laws and regulations relating to financial management at DLA (Project No. 6LA-2005). The Chief Financial Officers Act of 1990 (Public Law 101-576) established requirements for Federal organizations to submit audited financial statements to the Director, Office of Management and Budget. The Government Management Reform Act of 1994 (Public Law 103-356) required DoD and other Government agencies to prepare consolidated financial statements for FY 1996 and each succeeding year. The consolidated DoD financial statements for FY 1996 will include the financial statements for the DLA. For FY 1995, the Department of the Treasury required the DoD to prepare and submit adjusted trial balances. The consolidated DoD adjusted trial balances for FY 1995 included the adjusted trial balances for the DLA General Fund. This report discusses the DLA General Fund Equipment account. We have issued a final report on the general fund trial balance (Report No. 97-024) and a draft report on the preparation of the general fund financial statements. DLA reported total general fund assets valued at $1,807 million and general fund equipment valued at $411 million (22.7 percent) for yearend FY 1995, which becomes the beginning balance for FY 1996.

Audit Objective. The audit objective was to determine whether DFAS had implemented effective management control procedures and complied with laws and regulations in accounting for and reporting on certain accounting transactions. Specifically, we reviewed general ledger account code 150.000, "Equipment," in the FY 1995 DLA general fund adjusted trial balances.

Audit Results. The DFAS-Columbus Center erroneously reported the DLA General Fund Equipment account on the FY 1995 adjusted trial balances. As a result, the FY 1995 yearend balance of $411 million for the DLA General Fund Equipment account was misstated by at least $73.5 million (Finding A).

The DFAS-Columbus Center and DLA did not perform periodic comparisons of the DLA General Fund Equipment account with custodial records. As a result, the DLA General Fund Equipment account balance was not reliable, may be overstated by about $85 million ($57.8 million was also cited in Finding A) and was not readily auditable (Finding B). The management control program could be improved because we identified a material weakness related to identifying capital equipment purchased and the organization holding the equipment (Appendix A).

Summary of Recommendations. We recommend that the Director, DFAS-Columbus Center, adjust the DLA General Fund Equipment account balance to delete the Defense

Business Operations Fund equipment accounts. We recommend that the Directors, DLA, and DFAS-Columbus Center, provide equipment account balances to general fund organizations for annual reconciliations with actual custodial records.

Management Comments. The DLA concurred with the recommendation to annually reconcile its custodial records with the proprietary equipment account balance in the Defense Property Accounting System and estimated the completion by January 31, 1997. DLA also stated that the management control weakness would be reported in its Annual Statement of Assurance.

The DFAS concurred with the recommendation to adjust the general fund equipment account balance. DFAS stated that a working group audited the Capital Asset/Equipment balances on various non-Defense Business Operations Fund trial balances, and determined that the balances were erroneously reflected. It also stated that journal vouchers were prepared and processed before the end of FY 1996. DFAS also concurred with the recommendation to provide the proprietary equipment account balances to the general fund organizations. DFAS stated that the Defense Property Accounting System records were used to validate accounting records to equipment on hand per the activities' custodial equipment records. Journal vouchers were prepared and processed before the end of FY 1996. DFAS also stated that it will provide the general fund organizations copies of the account balances annually. Finally, DFAS stated that both actions were completed before September 30, 1996. See Part I for a discussion of management comments and Part III for the complete text of management comments.

Audit Response. The DLA comments were partially responsive. Although DLA concurred with the recommendation, it did not provide specific comments on the actions in process to resolve the problems identified. We request that DLA provide additional comments in its response to the final report by February 3, 1997.

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Part I - Audit Results

Audit Background

Public Law. The Chief Financial Officers Act of 1990 (the Act), Public Law 101-576, requires executive departments and agencies to prepare financial statements. The Act also requires inspectors general to audit or arrange for the audit of all financial statements prepared under the Act. The resulting audit reports must include an audit opinion of the financial statements, an assessment of the adequacy of internal controls of the reporting entity, and the compliance of an agency with laws and regulations that could have a material effect on the financial statements. The Act, as amended by the Federal Financial Management Act of 1994, assigns management the responsibility for the financial statements, internal controls, and compliance with laws and regulations. The Government Management Reform Act of 1994 (Public Law 103-356) required DoD and other Government agencies to prepare consolidated financial statements for FY 1996 and each succeeding year.

DoD Implementation. The Under Secretary of Defense (Comptroller) designates agencies and funds for which separate financial statements must be prepared. The preparation of the financial statements is the responsibility of the Defense Finance and Accounting Service (DFAS). In FY 1996, the Under Secretary of Defense (Comptroller) designated the category, "Other Defense Organizations," to prepare consolidated financial statements. General Fund appropriations of the Defense Logistics Agency (DLA) are included in the "Other Defense Organizations" category.

General Fund Defense Logistics Agency. The DLA General Fund appropriations for FY 1996 consist of Military Construction; Operation and Maintenance; Procurement, Defense-wide; and Research, Development, Test, and Evaluation. The General Fund appropriations are used mainly to support the activities of the Defense Contract Management Command (the Command). In FY 1996, about $779 million (70 percent) of the $1.1 billion DLA General Fund appropriations were used to support the Command. The Command provides worldwide contract administration services in support of DoD Components, other Federal agencies, and international organizations.

DoD Financial Management Regulation. DoD Regulation 7000.14-R, "DoD Financial Management Regulation," contains guidance on what constitutes a material deficiency in an accounting system. That regulation provides 13 key accounting requirements that systems must comply with to meet standards established by the General Accounting Office, Office of Management and Budget, the Department of the Treasury, and DoD. Specifically, key accounting requirement 2 states that the property management system must include accounting controls that identify the item, acquisition date, cost, its location, quantity, and other information.

Audit Objective

The audit objective was to determine whether the DFAS had implemented effective management control procedures and complied with laws and regulations in accounting for and reporting on certain accounting transactions. Specifically, we evaluated the effectiveness of accounting controls over general ledger account code 150.000, "Equipment" for the FY 1995 adjusted trial balances for the DLA General Fund. See Appendix A for a discussion of the scope and methodology and Appendix B for a summary of prior coverage related to the audit objective.

Finding A. Defense Logistics Agency General Fund Equipment

The DFAS-Columbus Center erroneously reported the DLA General Fund Equipment account on the FY 1995 adjusted trial balances. The account was erroneously reported because DFAS-Columbus Center did not make the appropriate accounting entries needed to delete the Defense Business Operations Fund (DBOF) equipment from the General Fund Equipment account. As a result, the FY 1995 yearend balance of $411 million for the DLA General Fund Equipment account was misstated by at least $73.5 million.

Financial Management Process

Financial Policy Guidance. The Under Secretary of Defense (Comptroller) issued, "Capital Asset Accounting Guidance for the Defense Business Operations Fund," July 21, 1992. The guidance provides that assets, acquired before October 1, 1990, are to be capitalized to the DBOF books and records and expensed over the useful life of the equipment. Capitalization is required because the equipment has a useful life of 2 or more years and meets an established dollar threshold requirement for capitalization.

Defense Business Operations Fund Organizations. Congress created DBOF on October 1, 1991, by combining the Defense and Service-owned stock and industrial funds. The Under Secretary of Defense (Comptroller) issued guidance requiring DBOF organizations to capitalize all assets to the DBOF equipment account, regardless of the source of acquisition funding.

Defense Business Management System. The Defense Business Management System (DBMS) is the accounting system that the DFAS-Columbus Center uses to record and analyze the DLA General Fund transactions. Within the DBMS, the account balance for capitalized assets is contained in general ledger account code 150.000 "Equipment." The DBMS rolls up the account balances of most General Fund Equipment accounts into subhead 5110. Although the subhead facilitates the consolidation of account balances, it does not represent an actual general fund organization.

Preparation of Financial Statements. The general ledger with the subsidiary accounts provides an integrated accounting and reporting structure. The trial balance is a summary of general ledger account balances for each accounting period (fiscal year). The general ledger account codes provide independent control over all assets, liabilities, revenues, expenses and budgetary resources. The monthly trial balances are considered interim financial reports for which account balances are reported for the accounting period.

Any out of balance accounts are adjusted and an adjusted trial balance is prepared listing the Standard General Ledger account and balances in numerical order, prepared at yearend. The adjusted trial balance is used to prepare the financial statements provided to the Under Secretary of Defense (Comptroller) for consolidation in the annual DoD financial statements. The consolidated DoD financial statements are submitted to the Department of the Treasury for the consolidated U.S. Government financial statements. For FY 1995, the Department of the Treasury required the DoD to prepare and submit adjusted trial balances. The consolidated DoD adjusted trial balances for FY 1995 included the adjusted trial balances for the DLA General Fund. DLA reported total general fund assets valued at $1,807 million and general fund equipment valued at $411 million for yearend FY 1995.

Subhead 5110

General Fund Appropriations in Subhead 5110. The DFAS-Columbus Center provided yearend FY 1995 adjusted trial balances for each general fund appropriation, specifically, Military Construction; Operation and Maintenance; Procurement, Defense-wide; and Research, Development, Test, and Evaluation. However, only three DLA trial balances reported General Fund Equipment: Operation and Maintenance $226.1 million, Procurement, Defense-wide $184.8 million, and Research, Development, Test, and Evaluation $0.1 million. DFAS-Columbus Center officials stated that the DBMS rolls up account balances into subhead 5110 on a daily basis, which causes difficulty in identifying assets in the individual reporting organizations. The rollup was not in compliance with key accounting requirement 2 of the DoD Financial Management Regulation. DFAS-Columbus Center identified the noncompliance as a deficiency in its annual statement of assurance (see Appendix A).

DFAS-Columbus Center Equipment Breakout. The DFAS-Columbus Center provided us a breakout of the General Fund Equipment account (see Appendix C), before its consolidation under subhead 5110. The General Fund Equipment breakout included a $470 million account balance. In Table 1, we adjusted the General Fund Equipment breakout to arrive at the DLA adjusted trial balance equipment amount.

Table 1. Subhead 5110 Equipment Account Rollup as Adjusted by Audit
(thousands)

Funds[1]	DFAS	Subtract	Add	ATB[2]
0100	$228,385	$ 2,545[3]	$229[4]	$226,069
0200	994	994[5]	-	0
0300	187,360	2,553[6]	-	184,807
0400	136	-	-	136
0510	53,415	53,415[6]	-	0
Total	**$470,290**	**$59,507**	**$229**	**$411,012**

[1]Operation and Maintenance (0100), Operation and Maintenance - Merge-Year account for Environmental Purposes (0200), Procurement (0300), Research, Development, Test, and Evaluation (0400), Base Realignment and Closure Account (0510)·
[2]Adjusted Trial Balances.
[3]Delete Defense Contract Audit Agency Operation and Maintenance funds.
[4]Add six organizations reported individually by DFAS.
[5]Did not receive a trial balance on 0200 funds.
[6]Deletion of DFAS Procurement and Base Realignment and Closure Account funds.

We adjusted the reported dollar values because the $470 million included on the General Fund Equipment breakout did not match the General Fund Equipment account on the adjusted trial balances. Specifically, to derive the reported adjusted trial balances we deleted the Defense Contract Audit Agency and DFAS because they were not DLA general fund organizations. Also, we included in the Operation and Maintenance adjusted trial balance six organizations that were not included in the subhead 5110 rollup. The six organizations were the Defense Contract Management District (DCMD)-Midatlantic (disestablished), the Defense Automatic Addressing System (DBOF organization), the DLA Finance Center, Defense Depot Ogden Utah (DBOF organization), the Industrial Plant Equipment/Defense Supply Center-Richmond (DBOF organization), and the Defense Civilian Personnel Management Services. Further, we deleted merge year (0200) funds because 0200 funds are not included on the list of general fund appropriations for DoD.

Misstated Account Balances

The DFAS-Columbus Center erroneously reported the DLA General Fund Equipment account on the FY 1995 adjusted trial balances by including DBOF equipment. The DBMS consolidated nine different databases under subhead 5110 to support the General Fund Equipment account, valued at approximately $411 million, for the FY 1995 adjusted trial balances (see Table 2). (Although Table 2 lists the primary organizations within each database, most of the entities are DBOF organizations).

Table 2. Adjusted Trial Balances by Appropriation
(millions)

Entity Name[1]	0100[2]	0300[3]	0400[4]	Total
DASC/DDRE	$ 30.6	$128.2	$0.1	$158.9
DCMDNE	11.8	7.5	-	19.3
DCMDS	17.6	-	-	17.6
DDMT	42.7	0.1	-	42.8
DDOU	16.8	18.1	-	34.9
DDRW/DCMDW	57.6	3.4	-	61.0
DESC	18.7	16.2	-	34.9
DPSC	25.7	0.2	-	25.9
DSCR	4.4	11.1	-	15.5
Other[5]	0.2	-	-	0.2
Total	**$226.1**	**$184.8**	**$0.1**	**$411.0**

[1]DASC/DDRE DLA Administrative Support Center (DBOF)/ Defense Distribution Region-East (DBOF).
DCMDNE Defense Contract Management District (DCMD)-Northeast.
DCMDS DCMD-South.
DDMT Defense Depot Memphis Tennessee (DBOF).
DDOU Defense Depot Ogden Utah (DBOF).
DDRW/DCMDW Defense Distribution Region-West (DBOF)/DCMD-West.
DESC Defense Electronics Supply Center (DBOF).
DPSC Defense Personnel Support Center (DBOF).
DSCR Defense Supply Center-Richmond (DBOF).
[2]0100 Operation and Maintenance.
[3]0300 Procurement, Defense-wide.
[4]0400 Research, Development, Test, and Evaluation.
[5]Other Equipment not in subhead 5110.

Defense Business Operations Fund Organizations. The DBOF organizations complied with the Under Secretary of Defense (Comptroller) guidance that required DBOF organizations to capitalize all assets to DBOF accounts regardless of the source of acquisition funding. However, the DBOF assets were not deleted from the DLA General Fund Equipment account. DFAS-Columbus Center officials could not explain why assets of DBOF organizations were listed in the General Fund Equipment account balance. We verified the equipment account balances for two DBOF organizations (Defense Distribution Region-West and Defense Supply Center-Richmond) and found potential misstatements. DLA informed us that the amount for "Other" equipment in Table 2 represented equipment for six organizations that should not have been included under subhead 5110.

Defense Distribution Region-West. The DBMS erroneously reported $61 million of general fund equipment in the general fund trial balance under the Defense Distribution Region West (a DBOF organization) and the DCMD-West (a general fund organization). Neither the Defense Distribution Region-West nor DCMD-West provided support for the $61 million. The Defense Distribution Region-West reported no general fund assets and the DCMD-West accounted for only $3.2 million.

The Defense Distribution Region-West provided a summary of capital equipment for both its DBOF trial balance and its custodial records as of February 29, 1996. The summary reported DBOF trial balance equipment valued at $129.2 million and custodial records equipment valued at $122.9 million. The Defense Distribution Region-West officials could not explain the difference between the DBOF trial balance and the custodial records. DLA personnel indicated that DLA assets were converted to the DBOF, as required. To determine whether the general fund equipment was properly converted and included on the DBOF trial balance, we selected three purchase orders for equipment purchased with general fund appropriations before the Defense Distribution Region-West was transferred to a DBOF organization. DLA traced the purchase orders and verified that they were recorded under Defense Distribution Region-West on the DBOF trial balance. We requested that DLA trace transactions because the DBMS did not comply with key accounting requirement 2.

The DCMD-West provided a list of equipment for which the unit cost exceeded $5,000. We compared each item on the list with the DoD criteria for capitalization and determined that $3.2 million of equipment on the list qualified as capital equipment. We were unable to reconcile the difference ($57.8 million) between the reported $61 million account balance and the $3.2 million of equipment on hand at DCMD-West.

Defense Supply Center-Richmond. The DBMS erroneously reported $15.5 million of general fund equipment in the general fund trial balance under the Defense Supply Center-Richmond (a DBOF organization). A Defense Supply Center-Richmond official informed us that all general fund equipment was converted to the DBOF and reported on the DBOF trial balance. However, a DFAS-Columbus Center official stated that a corresponding accounting entry to close the General Fund Equipment account balance was not made. We determined that the equipment was converted to DBOF accounts by selecting five acquisition transactions that were acquired before the Defense Supply Center-Richmond was transferred to a DBOF organization. A Defense Supply Center-Richmond official traced the five transactions and determined that all were recorded in the DBMS as DBOF assets. We had to trace transactions because the DBMS did not comply with key accounting requirement 2, which requires identification of general fund assets and their locations.

Other Organizations Included in General Fund Trial Balance. The DBMS individually identified six DLA organizations in the Operation and Maintenance appropriation, with account balances of approximately $0.2 million (listed as Other in Table 2), in the general fund trial balance. However, only one organization was appropriately reported (General Fund Equipment account balance of $55,864). The remaining five organizations were reported in error. Specifically, one organization was disestablished (General Fund Equipment account balance of $69,137), and four were DBOF organizations. Of the four DBOF organizations, three had a combined General Fund Equipment account balance of $117,062, and one had reported a negative account balance of $12,637 for equipment since FY 1992. The DFAS-Columbus Center could not explain why that organization reported negative assets.

Materiality and Impact on Financial Statements

The management controls over the General Fund Equipment account were materially deficient. The DoD Financial Management Regulation includes guidance on what constitutes a material deficiency in an accounting system. The Regulation provides 13 key accounting requirements that systems must reasonably comply with to meet standards established by the General Accounting Office, the Office of Management and Budget, the Department of Treasury, and DoD. Key accounting requirement 2 states that the property management system must include accounting controls that identify the item, cost, location, and other information.

Calculating Material Deficiency. According to the DoD Financial Management Regulation, a departure from a key accounting requirement is considered a material deficiency if it could result in a loss of control over 5 percent or more of the measurable resources for which the accounting system is responsible. At September 30, 1995, the DLA General Fund Equipment account reported a total balance of $411 million. Applying the noted materiality criteria of 5 percent to the DLA General Fund Equipment account would result in a material deficiency if an imbalance of $20.6 million or more was identified.

Material Deficiency in General Fund Equipment Account. The DFAS-Columbus Center did not identify and correct imbalances of $73.5 million for the databases included in the General Fund Equipment account. Specifically, the Defense Distribution Region-West/DCMD-West imbalance was $57.8 million, the Defense Supply Center-Richmond imbalance was $15.5 million, and the six DLA organizations, $0.2 million. Further, the statement was not accurate because the databases contained both asset balances for general fund and DBOF organizations. As a result, the internal control structure was materially deficient.

Recommendation for Corrective Action

A. We recommend that the Director, Defense Finance and Accounting Service-Columbus Center, adjust the Defense Logistics Agency General Fund Equipment account balance to delete the Defense Business Operations Fund equipment accounts.

Management Comments

The DFAS concurred, stating that a working group audited the Capital Asset/Equipment balances on various non-DBOF trial balances, and determined that the balances were erroneously reflected. DFAS also stated that journal vouchers were prepared and processed; and that required actions were completed before September 30, 1996.

Finding B. Management Controls Over General Fund Equipment Account

The DFAS-Columbus Center and DLA did not perform periodic comparisons of the DLA General Fund Equipment account with custodial records. The comparisons were not performed because the DFAS-Columbus Center accounting system did not permit the identification and location of general fund equipment as reported on the FY 1995 general fund trial balance. As a result, the DLA General Fund Equipment account balance was not reliable and was not readily auditable, and the three databases that we reviewed may be overstated by about $85 million. If not corrected by the end of FY 1996, the overstatement will affect the FY 1997 financial statements.

Controls Over Equipment Accountability

Internal Control Standards. The General Accounting Office published "Standards for Internal Controls in the Federal Government," 1983, which defines the minimum level of quality acceptable for internal control systems in operation and constitute the criteria for the evaluation of the systems. The specific standard, entitled "Access to and Accountability for Resources," requires periodic comparison of the resources (equipment) with the recorded accountability (in this case DBMS). The periodic comparison of financial records generated by an accounting system with equipment custodial records and on-hand equipment is a basic control technique to maintain the integrity of the information by helping to ensure that errors have not occurred.

Defense Business Management System. The DFAS-Columbus Center accounting system, DBMS, does not maintain general fund proprietary accounts at an organization level. Instead, the DBMS separates data by organizations and maintains the data in 19 databases. DFAS-Columbus Center officials stated that DBMS can identify neither the general fund assets included in the account balances nor the dollar value of equipment at general fund organizations.

Defense Property Accounting System. The Defense Property Accounting System is the new accounting system for all DoD real and personal property. The Defense Property Accounting System was selected as the DoD-wide solution to problems with financial accounting for real and personal property. Both DLA and DFAS-Columbus Center have reported material internal control weaknesses with inaccurate reporting of property (see Appendix A), which the Defense Property Accounting System is intended to correct.

Comparison of DLA General Fund Equipment With Custodial Records

The DFAS-Columbus Center and DLA did not perform periodic comparisons of the DLA General Fund Equipment account with custodial records. Specifically, the three DCMDs that we visited had not been provided nor asked to validate a copy of the trial balance from DFAS-Columbus Center depicting their reported accountability for equipment. DFAS-Columbus Center officials informed us that the DBMS could not provide information on capital equipment by organization; therefore, the DFAS-Columbus Center could not provide organizations with General Fund Equipment account balances for comparison with custodial records. Further, the DFAS-Columbus Center did not perform a thorough review of the general fund accounts because all efforts were directed toward the DBOF accounts.

Recorded Accountability. The DFAS-Columbus Center provided us an equipment breakout showing the organizations included in the General Funds Equipment account. We visited the DCMD-Northeast, the DCMD-South, and the DCMD-West and compared the recorded accountability, per the DBMS, with the equipment on hand, as reported on the organization's custodial equipment records. Table 3 depicts the comparison of the General Fund Equipment account, taken from the trial balance, with the equipment on hand, reported by the organizations.

Table 3. Comparison of Trial Balance With Equipment on Hand at DCMD
(millions)

	Northeast	South	West	Total
Trial Balance	$19.3	$17.6	$61.0	$97.9
On Hand	1.8	7.7	3.2	12.7
Difference	**$17.5**	**$9.9**	**$57.8**	**$85.2**
Percent of Trial Balance	**90.6**	**56.2**	**94.7**	**87.0**

DCMD-Northeast. The custodial equipment list of DCMD-Northeast contained $1.6 million of equipment qualified as capital equipment. The DCMD-Northeast database also accounted for $0.2 million of capital equipment at the Defense Contract Management Command-Philadelphia. Therefore, the General Fund Equipment account balance for those organizations was $1.8 million, or less than 10 percent of the reported $19.3 million account trial balance.

DCMD-South. The custodial equipment list of DCMD-South contained $6.6 million of equipment qualified as capital equipment. The DCMD-South database also accounted for $0.2 million and $0.9 million of capital equipment at the Defense Contract Management Command-Chicago and the Defense

Contract Management Command-Dallas, respectively. Therefore, the General Fund Equipment account balance for those organizations was $7.7 million, or less than 44 percent of the reported $17.6 million account trial balance.

DCMD-West. The custodial equipment list of DCMD-West contained $3.2 million of equipment qualified as capital equipment. Therefore, the General Fund Equipment account balance was $3.2 million, or less than 6 percent of the reported $61 million account trial balance.

The DCMD-West database also contained the Defense Distribution Region-West. The equipment reported on the DFAS-Columbus Center adjusted trial balance for the Defense Distribution Region-West exceeded the value of equipment on its custodial records by $6.3 million (see Finding A).

Implementation of Defense Property Accounting System. The Defense Property Accounting System was selected to correct the inaccuracies in recording assets DoD-wide, including general fund organizations. The implementation schedule for the Defense Property Accounting System, dated February 21, 1996, covered only 6 of the 19 DBMS databases and did not list any general fund organizations. However, the DCMD-Northeast and DCMD-West (general fund organizations) had implemented the Defense Property Accounting System and their personnel were attending training. Further, a DFAS-Columbus Center official stated that the revised completion date for full implementation of all 19 DBMS databases is the first quarter of the 1997 fiscal year.

Summary

The DFAS-Columbus Center did not provide proprietary equipment account balances to general fund organizations for comparison with actual custodial records because the DBMS could not separately identify general fund assets. The inability of DFAS-Columbus Center to identify assets and periodically compare the recorded accountability of the equipment account with custodial records was a material internal control deficiency. However, the DFAS-Columbus Center and DLA identified the material control weakness in their respective annual statements of assurance and were preparing a new system, the Defense Property Accounting System, to correct the deficiency.

We are not making a recommendation to perform a 100 percent reconciliation of account balances for FY 1996 because it is cost prohibitive and action is underway to account for equipment under the Defense Property Accounting System by FY 1997.

Recommendations for Corrective Action

B.1. We recommend that the Director, Defense Finance and Accounting Service-Columbus Center provide proprietary equipment account balances to general fund organizations as the Defense Property Accounting System is implemented, and thereafter annually.

B.2. We recommend that the Director, Defense Logistics Agency, require its general fund organizations to annually reconcile their custodial records with the proprietary equipment account balance in the Defense Property Accounting System.

Management Comments

Defense Finance and Accounting Service. The DFAS concurred with Recommendation B.1., stating that the Defense Property Accounting System records were used to validate the accounting records to the equipment on hand per the activities' custodial equipment records. Journal vouchers were prepared and processed before the end of FY 1996. DFAS also stated that it will provide the general fund organizations copies of the account balances annually. Finally, DFAS stated that actions were completed by September 30, 1996.

Defense Logistics Agency. The DLA concurred with Recommendation B.2. and stated that the estimated completion date of the ongoing action is January 31, 1997.

Audit Response

The DLA comments were partially responsive. DLA concurred with the recommendation and gave the estimated completion date; however, it did not state the planned action to be taken. Therefore, we ask DLA to provide additional comments in its response to the final report.

Part II - Additional Information

Appendix A. Audit Process

Scope

We reviewed the DFAS-Columbus Center adjusted trial balances for DLA FY 1995 General Fund Equipment account containing 19 databases. An inaccurate beginning account balance would affect the reliability of the DLA FY 1996 financial statements. The audit included the reported $411 million beginning account balance for general ledger account code 150.000 "Equipment". We reviewed purchase orders, trial balances and custodial records from FY 1992 through FY 1996 for nine active databases in DBMS that input to general ledger account code 150.000.

Use of Computer-Processed Data. The audit entailed the use of computer-processed financial data for general ledger account code 150.000. Evaluation of the computer-processed data was limited to a review of trial balances generated by the DBMS and custodial equipment lists provided by the four organizations that we visited. We tested the reliability of the summary information in the DBMS by comparing account totals by organizational database with the custodial records for the respective organizations included in the database. The balances did not match. Therefore, we determined that the DBMS did not contain reliable information for the account reviewed.

Audit Period, Standards, and Locations. We performed this financial related audit from January through August 1996. The audit was performed 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. Appendix D lists the organizations we visited or contacted.

Methodology

We judgmentally selected and tested 3 of the 19 databases (North, South, and West) located at the DCMD-Northeast, the DCMD-South and the DCMD-West because those were the DLA principal general fund organizations. We also selected and reviewed the databases containing the Defense Supply Center-Richmond (a DBOF organization) and the DCMD-West, which contains the Defense Distribution Region-West (a DBOF organization). We examined property accountability records and acquisition records for FY 1992 through FY 1996, and compared the amounts reported in the DBMS general fund databases. We also interviewed operating personnel about the recording and

reporting of equipment purchased with general fund appropriations. With the assistance of DLA personnel, we traced selected transactions. We did not use statistical sampling procedures to perform this audit.

Management Control Program

DoD Directive 5010.38, "Internal Management Control Program," April 14, 1987*, requires DoD organizations to implement management control programs to provide reasonable assurance that programs are operating as intended and to evaluate the adequacy of the controls.

Scope of Review of Management Control Program. We assessed the management control program regarding the implementation of control techniques in place to ensure that the DLA General Fund Equipment account was reliable and auditable in accordance with DoD guidance. We also reviewed the management self-evaluation of those management controls.

Adequacy of Management Controls. The audit identified a material management control weakness as defined by DoD Directive 5010.38. Controls were not effective to provide reasonable assurance that material misstatements in the equipment account would be prevented or detected in a timely manner. The DBMS could not provide information on capital equipment purchased or the organization holding the equipment. Recommendations A., B.1., and B.2., if implemented, will improve the reporting of the General Fund Equipment account. A copy of the report will be provided to the senior official responsible for management controls within DFAS.

Adequacy of Management's Self-Evaluation. The DFAS-Columbus Center and DLA identified financial accounting of capital equipment as part of an assessable unit and, in our opinion, correctly identified the risk associated with financial accounting of capital equipment as high. However, in their evaluations, the DFAS-Columbus Center and DLA did not identify the specific material management control weakness identified by the audit because their evaluations covered a much broader area.

The DFAS-Columbus Center reported two departures to General Accounting Office accounting principles, standards,and related requirements in its FY 1994 annual statement of assurance. The DFAS-Columbus Center reported that the Base Operating Support System (a DBMS subsystem) did not properly account for capital assets, and non-DBOF proprietary accounts were not maintained at an organizational level in DBMS. In its FY 1995 annual statement of assurance, the DFAS-Columbus Center reported that the Base Operating

*DoD Directive 5010.38 has been revised as "Management Control Program," August 26, 1996. This audit was performed under the April 1987 version of the Directive.

Support System did not meet all necessary requirements and could not be certified as complying with General Accounting Office accounting principles, standards, and related requirements.

The DLA reported inaccurate reporting of property, plant, and equipment on the FYs 1994 and 1995 financial statements as a material weakness, and reported a target completion date for implementation of the Defense Property Accounting System as FY 1996. Although the annual statements of assurance reported only the weakness on DBOF, the corrective action was also underway at the general fund organizations.

Appendix B. Summary of Prior Audits and Other Reviews

During the last 5 years, the DFAS and the Office of the Inspector General, DoD, issued reports on DLA and its field organizations. The following are the audits and reviews that may affect how financial data are collected, analyzed, and reported for the DLA general fund.

Inspector General, DoD

Inspector General, DoD, Report No. 97-024, "General Fund Trial Balance of the Defense Logistics Agency at September 30, 1995," November 15, 1996, stated that the DFAS-Columbus Center did not reconcile the DLA general ledger accounts before preparing and certifying the FY 1995 DLA trial balance. The DFAS-Columbus Center accounting system did not readily permit identification of imbalances. In addition, the DFAS-Columbus Center accounting system did not provide an adequate audit trail to identify the cause and to correct the imbalance. The report recommended that the DFAS-Columbus Center accelerate the schedule for implementing accounting system changes needed to readily identify and correct account imbalances and perform needed reconciliations to ensure that DLA FY 1996 financial statements will be more reliable. DFAS concurred with the recommendations stating that software would be installed to implement the DoD Standard General Ledger and allow segregation of proprietary accounts. The final report requested DFAS to provide clarification regarding the specific actions to identify and correct imbalances.

Inspector General, DoD, Report No. 93-174, "The Internal Management Control Program at the Defense Contract Management Command," September 30, 1993, stated that 23 Defense Contract Management Command districts and field offices did not adequately implement the Internal Management Control program. Also, the Command did not have a system to track costs for internal control functions such as risk assessments and control reviews. Of the risk assessments, 36 percent, were not properly completed, and 89 percent of the internal management control reviews were either not performed, not adequate, or not documented. The automated and manual risk assessment questionnaires for measuring vulnerability were inadequate and ineffective. The report made no recommendations because the Defense Contract Management Command was taking corrective action to address the deficiencies disclosed during the audit.

DFAS

The Richmond Detachment of DFAS Federal Managers' Financial Integrity Act Division "Evaluation of the Appropriated Accounting Sub-System of the Defense Business Management System at the Defense Finance and Accounting Service-Columbus Center, Columbus, Ohio," April 15, 1994, reported that the Appropriated Accounting System sub-system of the DBMS did not conform to the principles, standards, and related requirements of the General Accounting Office, Office of Management and Budget, and DoD. The report stated that internal controls were insufficient, reconciliations performed in the Accounting Operations Division were inconsistent among the branches and did not normally address the quality of financial data. Also, many work areas lacked standard operating procedures, and the DBMS did not use the standard general ledger. DFAS concurred and identified planned corrective actions and completion dates.

The Richmond Detachment of DFAS Federal Managers' Financial Integrity Act Division "Evaluation of the Payroll Sub-System of the Automated Payroll, Cost and Personnel System," September 4, 1992, stated that DBMS Payroll sub-system did not conform to the principles, standards, and related requirements of the General Accounting Office, Office of Management and Budget, and DoD. Payroll totals were not in balance with payroll certifications, and the Payroll for Personnel Services Certification did not agree with disbursements. DFAS concurred and provided estimated completion dates for corrective actions.

Appendix C. General Fund Equipment Breakout

Subhead 5110[1] Equipment Account Rollup
(thousands)

Entity Name	Appropriation Codes[2] 0100	0200	0300	0400	0510	Total
Defense Contract Audit Agency	$ 2,545	$ 0	$ 0	$ 0	$ 0	$ 2,545
DFAS	0	0	2,553	0	53,415	55,968
DLA:						
DLA Administrative Support Center/ Defense Depot Region East	30,565	0	128,162	136	0	158,863
DCASR[3] Boston/New York	11,781	0	7,565	0	0	19,346
DCASR Atlanta/Chicago	17,639	0	0	0	0	17,639
Defense Construction Supply Center	0	0	0	0	0	0
Defense Depot Memphis Tennessee	42,710	0	56	0	0	42,766
Defense Depot Ogden Utah	16,834	0	18,115	0	0	34,949
Defense Depot Tracy California/ DCASR New York[4]	57,632	0	3,381	0	0	61,013
Defense Electronics Supply Center	18,661	0	16,197	0	0	34,858
Defense Personnel Supply Center	25,640	994	230	0	0	26,864
Defense Supply Center-Richmond	4,378	0	11,101	0	0	15,479
Total	**$228,385**	**$994**	**$187,360**	**$136**	**$53,415**	**$470,290**

1 Subhead that consolidates (rolls up) the General Fund appropriation codes.
2 Operation and Maintenance (0100), Operation and Maintenance - Merge-Year account for Environmental Purposes (0200), Procurement (0300), Research, Development, Test, and Evaluation (0400), Base Realignment and Closure Account (0510).
3 DCASR: Defense Contract Administration Services Region.
4 Erroneous entry, it should be Los Angeles.

Appendix D. Organizations Visited or Contacted

Defense Organizations

Defense Finance and Accounting Service-Columbus Center, Columbus, OH
Defense Logistics Agency, Fort Belvoir, VA
- Defense Contract Management Command, Fort Belvoir, VA
  - Defense Contract Management Command, International Office, Dayton, OH
  - Defense Contract Management District-Northeast, Boston, MA
  - Defense Contract Management District-South, Atlanta, GA
  - Defense Contract Management District-West, Los Angeles, CA
- Defense Distribution Region-West, Stockton, CA
- Defense Electronics Supply Center, Dayton, OH
- Defense Supply Center-Richmond, Richmond, VA

Appendix E. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense for Acquisition and Technology
  Director, Defense Logistics Studies Information Exchange
Under Secretary of Defense (Comptroller) and Chief Financial Officer
  Deputy Chief Financial Officer
  Deputy Comptroller (Program/Budget)
  Director for Accounting Policy
Under Secretary of Defense for Policy
Assistant Secretary of Defense for International Security Affairs
Assistant to the Secretary of Defense (Public Affairs)

Department of the Army

Auditor General, Department of the Army

Department of the Navy

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

Department of the Air Force

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

Other Defense Organizations

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

Non-Defense Federal Organizations and Individuals

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

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

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

Part III - Management Comments

Defense Logistics Agency Comments

DEFENSE LOGISTICS AGENCY
HEADQUARTERS
8725 JOHN J. KINGMAN ROAD, SUITE 2533
FT. BELVOIR, VIRGINIA 22060-6221

IN REPLY REFER TO DDAI

November 7, 1996

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING, DEPARTMENT OF DEFENSE

SUBJECT: OIG Draft Report, "*DLA General Fund Equipment Account*," **(Project No. 6LA-2005-02)**

This is in response to subject draft report dated September 5, 1996. If you have any questions, please contact Elaine Parker, DDAI at (703) 767-6264.

OLIVER E. COLEMAN
Acting Chief, Internal Review Office

Encl

Federal Recycling Program Printed on Recycled Paper

Subject: DRAFT REPORT: Defense Logistics Agency General Fund Equipment Account (Project No. 6LA-2005.02)

Finding: B. Management Controls Over General Fund Equipment Account. The DFAS-Columbus Center and DLA did not perform periodic comparisons of the DLA General Fund Equipment account with custodial records. The comparisons were not performed because the DFAS-Columbus Center accounting system did not permit the identification and location of general fund equipment as reported on the FY 1995 general fund trial balance. As a result, the DLA General Fund Equipment account balance was not reliable and was not readily auditable, and the three databases that we reviewed may be overstated by about $85 million. If not corrected by the end of FY 1996, the overstatement will affect the FY 1997 financial statements.

DLA Comments: Concur.

Internal Management Control Weakness:
Concur; weakness will be reported in the DLA Annual Statement of Assurance.

Action Officer: Richard Sninsky, FOXS
Review/Approval: B.A. Blackman, FOX
Coordination: James O'Laughlin, FOXS
Elaine Parker, DDAI

DLA Approval:

Subject: DRAFT REPORT: Defense Logistics Agency General Fund Equipment Account (Project No. 6LA-2005.02)

Recommendation No. B.2.: We recommend that the Director, Defense Logistics Agency, require its general fund organizations to annually reconcile their custodial records with the proprietary equipment account balance in the Defense Property Accounting System.

DLA Comments: Concur.

Disposition: Action is ongoing. ECD: 31 January 1997

Action Officer: Richard Sninsky, FOXS
Review/Approval: B.A. Blackman, FOX
Coordination: James O'Laughlin, FOXS
Elaine Parker, DDAI

DLA Approval:

Defense Finance and Accounting Service Comments

DEFENSE FINANCE AND ACCOUNTING SERVICE

1931 JEFFERSON DAVIS HIGHWAY
ARLINGTON, VA 22240-5291

DFAS-HQ/AFB

NOV 13 1996

MEMORANDUM FOR DIRECTOR, LOGISTICS SUPPORT, OFFICE OF THE INSPECTOR GENERAL, DEPARTMENT OF DEFENSE

SUBJECT: Management Comments on DoDIG Draft Audit Report, "Defense Logistics Agency General Fund Equipment Account," dated September 5, 1996 (Project No. 6LA-2005.02)

Our comments on the subject report are attached.

Please direct any questions concerning this matter to Mr. Charles McIntosh on (703) 607-5105.

Thomas F. McCarty
Deputy Director for
Accounting

Attachment

Final Report Reference

RECOMMENDATION A: We recommend that the Director, Defense Finance and Accounting Service-Columbus Center, adjust the Defense Logistics Agency General Fund Equipment account balance to delete the Defense Business Operations Fund equipment accounts.

Management comments: Concur. A working group was established to audit Capital Asset/Equipment balances on various non-DBOF Trial Balances. It was determined that the balances were erroneously reflected on these as well as the DBOF Trial Balances. Journal Vouchers (copies attached) were prepared and processed prior to the end of fiscal year 1996.

Attachment deleted

Estimated Completion Date: Required actions were completed prior to September 30, 1996.

RECOMMENDATION B1: We recommend that the Director, Defense Finance and Accounting Service-Columbus Center provide proprietary equipment account balances to general fund organizations as the Defense Property Accounting System is implemented, and thereafter annually.

Management comments: Concur. The Defense Property Accounting System records for Defense Contract Management District-East and Defense Contract Management District-West were used to validate accounting records to equipment on hand per the activities' custodial equipment records. Due to the disestablishment of Defense Contract Management District-South, the accounting records were validated to equipment on hand. Journal Vouchers (copies attached) were prepared and processed prior to the end of fiscal year 1996. We will provide the general fund organizations copies of the account balances annually.

Attachment deleted

Estimated Completion Date: Actions were completed prior to the end of fiscal year 1996.

Attachment

Audit Team Members

This report was prepared by the Logistics Support Directorate, Office of the Assistant Inspector General for Auditing, DoD.

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Dorothy L. Jones
Linda A. Garner