

Audit



Report

OFFICE OF THE INSPECTOR GENERAL

GENERAL FUND TRIAL BALANCE OF THE DEFENSE
LOGISTICS AGENCY AT SEPTEMBER 30, 1995

Report No. 97-024

November 15, 1996

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Department of Defense

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Acronyms

DBMS	Defense Business Management System
DFAS	Defense Finance and Accounting Service
DLA	Defense Logistics Agency



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November 15, 1996

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

SUBJECT: Audit Report on the General Fund Trial Balance of the Defense Logistics Agency at September 30, 1995 (Report No. 97-024)

We are providing this report for review and comment. This report 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). Management comments on a draft of this report were considered in preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. Although the Defense Accounting and Finance Service concurred with the recommendations, we request clarification on certain matters. The comments do not state how actions taken will help identify and correct account imbalances. In addition, although the Defense Finance and Accounting Service states that reconciliations have been performed, the specific account imbalances identified by the report have not been reconciled. We request that the Defense Finance and Accounting Service provide additional comments in its response to the final report by January 15, 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 F for the report distribution. The audit team members are listed on the inside back cover.

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Office of the Inspector General, DoD

Report No. 97-024
(Project No. 6LA-2005.01)

November 15, 1996

General Fund Trial Balance of the Defense Logistics Agency at September 30, 1995

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 the 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 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. This report discusses the adequacy and usefulness of the General Fund Trial Balance process supporting the FY 1995 DLA financial statements. This report also discusses the impact of the General Fund Trial Balance process on the DLA financial statements for FYs 1996 and 1997. The DLA FY 1995 appropriations totaled about \$1.9 billion. Because about 87 percent of the FY 1995 general funds consisted of an Operation and Maintenance appropriation, we evaluated the DLA trial balance for operation and maintenance. The DFAS-Columbus Center is responsible for maintaining the accounting system for funds DLA manages.

Audit Objectives. The primary audit objective was to determine whether DFAS had implemented effective management control procedures and complied with laws and regulations in preparing financial statements for DLA. The specific objective of this report was to assess the reliability of the DLA trial balance used in preparing the DLA financial statements.

Audit Results. The DFAS-Columbus Center did not reconcile the DLA general ledger accounts before preparing and certifying the FY 1995 DLA trial balance. Specifically, the DFAS-Columbus Center had not identified and corrected imbalances of \$543 million between the general and supporting subsidiary ledgers and \$894 million between equivalent proprietary and budgetary general ledger accounts. Although we determined the imbalances, 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 of and correct the imbalance. As a result, the DLA trial balance amounts were not reliable and not auditable, and there was no assurance that the resultant financial statements of DLA were accurate.

The management controls we reviewed were inadequate because of a material weakness in the DFAS implementation of changes in the accounting system for the DLA general funds. Implementation of the recommendations will improve the accounting system. See Part I for a discussion of the audit results.

Summary of Recommendations. We recommend that the Director, DFAS-Columbus Center, accelerate the implementation of 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.

Management Comments. The DFAS concurred with the recommendations. DFAS stated that software would be installed to implement the DoD Standard General Ledger and allow segregation of proprietary accounts. In addition, DFAS stated that multiple reconciliations are currently performed and that it hopes to complete its search for tools to enhance the reconciliation process by October 31, 1996. See Part I for a discussion of management comments and Part III for the complete text of those comments.

Audit Response. The DFAS comments did not indicate how the actions taken would more readily allow the identification of imbalances and correct identified imbalances. In addition, although DFAS indicated that reconciliations have been completed, its comments testify that it has not reconciled the imbalance between proprietary and budgetary equivalents. We request that DFAS provide clarification in its response to the final report by January 15, 1997.

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Part I - Audit Results

Audit Background

The audit was performed as part of the Audit of Financial Management at the Defense Logistics Agency (Project No. 6LA-2005). This report is one in a series of reports. 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. Public Law 103-356, "The Management Reform Act of 1994," 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 Defense Logistics Agency (DLA).

Defense Logistics Agency. The DLA is a combat support agency responsible for worldwide logistics support throughout DoD. The Defense Contract Management Command is a major business element of the DLA that performs most DoD contract administrative services and administers most DoD contracts on behalf of foreign governments. The Defense Contract Management Command received the majority of the DLA FY 1995 general funds to monitor and manage about 450,000 prime contracts valued at more than \$770 billion. DLA received general funds from seven appropriations in FY 1995. Of the \$1.9 billion general funds appropriated in FY 1995, \$1.7 billion (87 percent) was Operation and Maintenance funds. DLA, as the funds manager, is responsible for establishing and maintaining an internal control structure applicable to those funds. Appendix B lists the nine sources and amounts of the DLA FY 1995 general funds.

Defense Finance and Accounting Service. DoD Regulation 7000.14R, volume 1, "Financial Management Regulation; General Financial Management Information, Systems, and Requirements," May 1993, (DoD Financial Management Regulation) assigns the Defense Finance and Accounting and Service (DFAS) as the accounting entity for DoD. As a result, DFAS is responsible for compliance with applicable laws and regulations when providing accounting support and managing the accounting system for the DLA general fund.

Defense Business Management System. The Defense Business Management System (DBMS) is an accounting system used to record, analyze, process, and report DLA general fund transactions. DFAS, Headquarters, was responsible for managing DBMS through the end of FY 1995. DFAS, Headquarters, assigned the responsibility of managing the DBMS to the DFAS-Columbus Center on October 1, 1995.

Audit Objective

The primary audit objective was to determine whether DFAS had implemented effective management control procedures and complied with applicable laws and regulations in preparing financial statements for DLA. The specific objective of this report was to assess the reliability of the DLA trial balance when preparing the DLA financial statements. See Appendix A for a discussion of the scope, methodology, and the review of the management control program and a summary of prior coverage related to the audit objectives.

Defense Logistics Agency Trial Balance

The DFAS-Columbus Center did not reconcile imbalances in the DLA general ledger accounts before preparing and certifying the FY 1995 DLA trial balance. Specifically, DLA imbalances of \$543 million between the general and supporting subsidiary ledgers and \$894 million between equivalent proprietary and budgetary general ledger accounts were not reconciled. The imbalances were not reconciled because DFAS had not implemented accounting system changes to readily allow identification of account imbalances and to provide the audit trail needed to correct identified imbalances. As a result, certain DLA trial balance amounts were not reliable and not auditable; and there was no assurance that the resultant financial statements of DLA were accurate.

General Ledger Accounts

The trial balance is the summary of all the general ledger accounts. The accuracy of the trial balance information is crucial to the preparation of the financial statements. As a minimum, if the trial balance at year-end (September 30th) is unreliable the accuracy of the current year financial statement is questionable. Further, since the year-end balance is the next year's beginning balance, the unreliable data affect the subsequent year's financial statement; especially if the causes for inaccurate data are not corrected. DoD Financial Management Regulation requires monthly reconciliation of general ledger account equivalents to help ensure the accuracy of the financial information. The Joint Financial Management Improvement Program, "Core Financial System Requirements," Federal Financial Management System Requirements Number 1, September 1995, states that to adequately reconcile, an accounting system should have the capability for management to readily identify and correct general ledger imbalances. To readily identify account imbalances, an accounting system must report the imbalances. To research and correct an imbalance, an accounting system should provide an audit trail to determine the causes of the imbalances.

Management of the General Ledger Accounts. Management of the general ledger account is the central function of the financial accounting system. The general ledger is the highest level of account summarization and should include all financial transactions. To ensure that all financial transactions are included

accurately in the general ledger, reconciliations should be performed periodically with the supporting subsidiary ledgers and between proprietary¹ and budgetary² general ledger account equivalents.

Subsidiary Ledgers. Subsidiary ledgers are to provide, at various levels of detail, support for general ledger account balances. If subsidiary ledger amounts do not agree with amounts recorded in the general ledger accounts, an imbalance exists.

Proprietary and Budgetary General Ledger Equivalents. The DBMS has proprietary and budgetary equivalents. For example, the DBMS has two proprietary general ledger cash accounts that should equal two budgetary general ledger cash accounts. Specifically, the DBMS proprietary general ledger accounts 111.000 and 112.000 should equal the DBMS budgetary general ledger accounts 471.000 and 472.000, respectively. If proprietary and budgetary general ledger equivalents are not in agreement, an imbalance exists.

Audit Trail. An audit trail is necessary to determine the causes of account differences. Adequate audit trails are critical to providing support for transactions and balances maintained by the accounting system. The accounting system must provide audit trails to trace transactions from source documents, original input, other systems, system-generated transactions, and internal allocation transactions through the system; to trace source documents through successive levels of summarization to financial statements and the reverse; and to identify changes made to system parameters and tables that affect the processing of any financial transactions. The accounting system should also provide the ability to select items for review based on user defined criteria. Audit trails are necessary for the day-to-day monitoring of the accounting system. For example, an effective audit trail will facilitate the detection and systemic correction of errors that arise.

DFAS Knowledge of Reconciliation Weaknesses. The DFAS-Columbus Center developed plans to improve the ability of the accounting system to reconcile general ledger accounts. Specifically, system change requests were developed in June 1994 to create an automated process to facilitate the reconciliation of general ledger accounts with subsidiary ledgers and to prepare Operation and Maintenance trial balances by organization to facilitate the

¹Proprietary accounts are general ledger accounts used to track the balances of assets, liabilities, net position, revenues, and expenses.

²Budgetary accounts are general ledger accounts used to track the effects of financial events on the sources and uses of budgetary resources, commonly referred to as budget execution.

Defense Logistics Agency Trial Balance

required reconciliations.³ In addition, the DFAS-Columbus Center accounting and training divisions were looking at automating the reconciliation of proprietary and budgetary general ledger equivalents.

Reconciliation of General Ledger

The DFAS-Columbus Center had no basis for certifying that the FY 1995 DLA trial balance amounts were correct and supported by subsidiary ledgers. The DFAS-Columbus Center did not reconcile general ledgers with supporting subsidiary ledgers and proprietary and budgetary general ledger account equivalents before preparing and certifying the FY 1995 DLA trial balance. Specifically, the DFAS-Columbus Center had not identified and corrected an imbalance of \$543 million between general ledger and subsidiary ledgers, and \$894 million between proprietary and budgetary equivalents (see Appendixes C and D, respectively). The DFAS-Columbus Center accounting system (the DBMS) did not readily allow reconciliation.

Accounting System Changes

Although the DFAS-Columbus Center had plans to improve the accounting system for more ready reconciliation, the needed changes to the accounting system had not been implemented as of May 1996. Specifically, the system change requests of the DFAS-Columbus Center to automate reconciliation of general ledger accounts with subsidiary ledgers and to prepare Operation and Maintenance trial balances by activity to facilitate the required reconciliations, had not been implemented.⁴ In addition, the DFAS-Columbus Center was looking at how to best automate the reconciliation of proprietary and budgetary equivalents, but had not implemented any changes. Accounting system changes are needed to be implemented to more readily allow the identification of account imbalances and to provide the needed audit trail to correct identified imbalances.

³The two system change requests were in response to a DFAS Richmond Detachment report, "Evaluation of the Appropriated Accounting Sub-system of the Defense Business Management System (DBMS) at the Defense Finance and Accounting Service, Columbus Center, Columbus, Ohio," (see Appendix A for further details on DFAS report).

⁴The system change request to automate reconciliation of general ledgers with subsidiary ledgers had not been scheduled for implementation. However, the system change request to prepare trial balances by activity is scheduled to begin testing in May 1997.

Identification of Imbalances in Accounts. Excessive manual effort and coordination were required to identify the imbalances between general and subsidiary ledgers and proprietary and budgetary equivalents.

General and Subsidiary Ledgers. The auditors, with DFAS-Columbus Center assistance, had to manually search, identify, collect, extract, and compile needed subsidiary ledgers from various microfiche media for 62 DLA activities to identify the \$543 million imbalance between general and subsidiary ledgers. In addition, because there were different identifying codes between the general ledger and supporting subsidiary ledgers, various crosswalk tables were required to determine whether a specific subsidiary ledger supported the general ledger in question. Periodically, DFAS personnel were required to provide the needed crosswalk information because the tables failed to provide equivalent activity codes between general and subsidiary ledgers.

Proprietary and Budgetary General Ledger Account Equivalents. The auditors had to manually search, identify, collect, extract, and compile needed information from more than 310 trial balance reports to determine the \$894 million imbalance between proprietary and budgetary general ledger account equivalents. In addition, to ensure that our formulas of proprietary and budgetary equivalency were correct and that all trial balance reports were appropriately included, we consulted with DFAS-Columbus Center personnel in three divisions. After the consultation, the DFAS-Columbus Center officials could not definitively state that we had included all needed trial balance reports.

Audit Trails to Correct Imbalances. The DBMS did not have the capability to research and correct an imbalance between general and subsidiary ledgers and between proprietary and budgetary equivalents. Specifically, the accounting system did not provide an adequate audit trail to determine the causes of the out of balance conditions.

General Ledger to Subsidiary Ledger Audit Trail. The DFAS accounting officials supported only a portion of the general ledger total and stated that of the \$671 million in the FY 1995 general ledger expense account, only \$159 million was supported by a subsidiary ledger. The remaining \$512 million was rolled directly into the DLA trial balance with no source documentation in support of the amount. A DFAS-Columbus Center accounting official stated that the \$512 million was the result of prior year unliquidated obligations being expensed in the current year. Those expenses were rolled into the DLA trial balance with no source and specific transaction documentation.

Subsidiary Ledger to Supporting Transactions. We identified no audit trail to source documentation supporting subsidiary ledger amounts. For example, we selected four transactions from the transaction history of the subsidiary ledger for accounts receivable. The four transactions represented \$18 million (27 percent) of the \$65 million in the subsidiary ledger (see Appendix E for details). The DFAS-Columbus Center had not attempted to reconcile the trial balance to the subsidiary ledger and could produce no supporting documentation to validate existence of the receivables.

Defense Logistics Agency Trial Balance

Proprietary and Budgetary General Ledgers. The DBMS did not allow the selection of items for review based on user defined criteria. Specifically, the DBMS did not allow reconciliation at the agency organizational level. Of the 180 DLA organizations we reviewed, only 56 had individual proprietary trial balances. The DBMS consolidated the proprietary accounts of the remaining 124 DLA organizations into 10 summary trial balances. As a result, DFAS could not isolate account variances to smaller components to assist in reconciling the proprietary and budgetary general ledger accounts.

Accuracy of DLA Financial Statements

The DLA trial balance amounts were questionable and not auditable. As a result, there was no assurance that the DLA financial statements were accurate. The trial balance was questionable and not auditable because of unreconciled differences of \$543 million between selected general ledgers and their subsidiary ledgers and \$894 million between proprietary and budgetary equivalents. In addition, the existence of accounts receivables totaling at least \$18 million could not be determined. Because the accuracy of trial balance information is crucial to the preparation of financial statements, there was no assurance that the DLA financial statements were accurate. The causes for the imbalances in the financial records, unless corrected, will affect the FY 1996 and FY 1997 financial statements.

Materiality and Impact on Financial Statements

The management controls over general ledger accounts were materially deficient. The DoD Financial Management Regulation contains guidance on what constitutes a material deficiency in an accounting system. The regulation provides 13 key accounting requirements that systems must be in reasonable compliance with to meet standards established by the General Accounting Office, the Office of Management and Budget, the Department of the Treasury and the DoD.

Accounting Requirements. Key accounting requirement number 7 states that the accounting system must have adequate internal controls to prevent, detect, and correct errors and irregularities that may occur throughout the system.

Calculating Material Deficiency. According to the DoD Financial Management Regulation, a departure from a key accounting requirement is considered a material deficiency if the departure could result in 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 Trial Balance reported a total balance of \$19.9 billion. Applying the noted materiality criteria of 5 percent to the DLA trial balance would mean a material deficiency would occur if an imbalance of \$997 million or more was identified.

Material Deficiency in General Ledger. The DFAS-Columbus Center did not identify and correct general ledger imbalances of \$1.4 billion (\$543 million between the general and subsidiary ledgers, and \$894 million between the proprietary and budgetary equivalent accounts). As a result, the management control structure was materially deficient.

Management Comments on the Finding and Audit Response

Management Comments. The DFAS provided comments on the materiality of the imbalance. DFAS stated that contrary to the imbalance of \$894 million between proprietary and budgetary equivalents identified by the audit, the DFAS-Columbus Center calculated an imbalance of \$309 million for the same equivalents. It stated that the differences were due to different methods of calculation. The DFAS-Columbus Center netted account differences and the IG, DoD, totaled account differences. For example, if one DLA trial balance had a \$200,000 difference between proprietary and budgetary equivalents and another complimentary DLA trial balance had (-)\$100,000 difference between the same equivalents, the DFAS-Columbus Center netted the differences and calculated the imbalance at \$100,000. In contrast, the IG, DoD, totaled the differences and calculated the imbalance at \$300,000. DFAS also stated that whichever methodology is appropriate, it is committed to identifying and correcting the cause of the imbalance. DFAS stated that it is trying to determine the cause of the imbalance and resolve it.

Audit Response. We believe imbalance differences should be totaled, because netting differences between trial balances assumes that the cause of a positive difference in one trial balance is the cause of a negative difference in another trial balance. DFAS had not determined the cause of the imbalance. Netting differences without knowing the cause results in inadequate accounting system internal controls within an accounting system. Key accounting requirement number 7 states that an accounting system must have adequate internal controls to detect irregularities that may occur throughout the system. Netting differences between trial balances results in avoiding the detection of irregularities. However, if DFAS continues to net account differences, it should disclose that fact in its financial statements. We request that DFAS provide additional comments in response to the final report.

Recommendations, Management Comments, and Audit Response

We recommend that the Commander, Defense Finance and Accounting Service-Columbus Center:

1. Accelerate the implementation of accounting system changes to readily allow identification of account imbalances and to provide the needed audit trail to correct identified imbalances.

Management Comments. The DFAS concurred with the recommendation stating that a Defense Business Management System software release 9.000 is estimated to be installed by July 31, 1997. The DFAS stated that the release 9.000 will implement the DoD Standard General Ledger and permit segregation of general fund proprietary accounts.

Audit Response. Although DFAS concurred with the recommendation, we do not consider its comments responsive. We agree that being able to segregate general fund proprietary accounts will help provide the needed audit trail to correct proprietary and budgetary imbalances. However, DFAS did not indicate how the actions taken would more readily allow for the identification of proprietary and budgetary account imbalances. In addition, DFAS did not indicate how the actions taken would more readily allow for the identification of account imbalances between general and supporting subsidiary ledgers and provide the needed audit trail to correct the identified imbalances. We request that DFAS reconsider its position and provide additional comments in its response to the final report.

2. Reconcile accounts so that the Defense Logistics Agency FY 1996 financial statements can be more reliable.

Management Comments. The DFAS concurred with the recommendation, stating that DFAS-Columbus Center currently performs multiple reconciliations of abnormal balances and imbalances of general and subsidiary accounts. The DFAS stated that it is looking at ways to enhance the reconciliation process and estimated a completion date of October 31, 1996, for looking for new tools.

Audit Response. Although DFAS concurred with the recommendation, we do not consider its comments responsive. DFAS did not comment on when it will reconcile account imbalances, but stated that it currently performs multiple reconciliations. DFAS also stated that it was trying to determine the cause of the imbalance in proprietary and budgetary equivalents. Accordingly, DFAS should proceed in determining the cause for the account imbalances. We request that DFAS reconsider its position and provide additional comments in its response to the final report, including an identification of the new tools it will use in the reconciliation process.

Part II - Additional Information

Appendix A. Audit Process

Scope

We reviewed the DFAS process for developing a trial balance for DLA general funds at September 30, 1995. We evaluated the DLA trial balance for the Operation and Maintenance appropriation because about 87 percent of the DLA FY 1995 general funds consisted of an Operation and Maintenance appropriation. Documents reviewed were DBMS proprietary and budgetary trial balance reports (UPFE600A, UPFE650A, UPFZ700A, and UPFZ750A) dated September 30, 1995; and DBMS subsidiary ledger reports (UPFE200A and UPFE300B) dated September 30, 1995. We determined whether reconciliations were performed between selected proprietary general ledger accounts and associated subsidiary ledgers and between proprietary and budgetary general ledger account equivalents. In addition, we evaluated four transactions supporting general ledger dollar amounts to determine whether they were supported by source documentation.

Use of Computer-Processed Data. To achieve the audit objective, we relied on the FY 1995 DLA trial balance generated by the DBMS accounting subsystem. As discussed in the report, we could not assess the reliability of the trial balance because an audit trail did not exist.

Audit Period, Standard, and Locations. We performed this financial-related audit from January through May 1996, 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 F lists the organizations visited or contacted.

Methodology

To determine whether reconciliations were performed between general and subsidiary ledgers, we interviewed DFAS-Columbus Center officials and calculated the subsidiary ledger totals that should support the general ledger accounts. We calculated the subsidiary ledger totals supporting the general ledger accounts for receivables and expenses within the DBMS central data base because it was the single largest data base applicable to the DLA Operation and Maintenance appropriation. We calculated the subsidiary totals by manually searching, identifying, collecting, extracting, and compiling needed subsidiary ledgers from various microfiche media for 62 DLA activities.

To determine whether reconciliations were performed between proprietary and budgetary general ledger equivalents, we interviewed DFAS-Columbus Center officials and calculated the DLA budgetary equivalent amounts for eight proprietary general ledger accounts summarized in the DLA trial balance. Because DLA budgetary amounts were not summarized, we calculated the budgetary amounts for proprietary equivalents by manually searching, identifying, collecting, extracting, and compiling needed budgetary amounts from more than 310 DLA activity trial balances.

To determine whether source documentation supported general ledger dollar amounts, we selected four transactions supporting the general ledger account for receivables within the DBMS central data base. Four transactions were selected based on the relative high dollar amount (\$18 million, 27 percent of the \$65 million in accounts receivables). Supporting documentation was determined by interviewing DFAS-Columbus Center officials.

We presented our results, conclusions, and methodology in determining whether reconciliations were being performed between general and subsidiary ledgers and between proprietary and budgetary general ledger equivalents and whether source documentation supported general ledger dollar amounts to DFAS-Columbus Center accounting officials for their review and comment.

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

Management Control Program

DoD Directive 5010.38,* "Internal Management Control Program," April 14, 1987, 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 Management Control Program. We assessed the management control program regarding the implementation of control techniques in place to ensure that the DLA trial balance was reliable and auditable in accordance with DoD guidance. We also reviewed management's self-evaluation of those management controls.

Adequacy of Management Controls. We identified a material management control weakness as defined by DoD Directive 5010.38. Although DFAS had identified weaknesses in the ability to identify and reconcile imbalances between control and subsidiary accounts in FY 1993, DFAS had not implemented the needed changes to the accounting system for DLA general funds. The

*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.

Appendix A. Audit Process

DFAS-Columbus Center scheduled one corrective change to be implemented during May 1997; another one has not yet been scheduled. As a result, the FYs 1996 and 1997 DLA Financial Statements may not be auditable. The recommendations in this report, if implemented, will improve the usefulness and reliability of the DLA FY 1996 and subsequent years general fund financial statements. 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, Headquarters, identified the reconciliation of the general ledger to supporting subsidiary ledgers and the existence of audit trails from financial statements to source documents as assessable units within the DBMS. DFAS, Headquarters, personnel conducted an evaluation for FY 1995, but did not identify the material weakness identified by the audit because their evaluation emphasized the DBMS capabilities to perform the accounting functions for the Defense Business Operations Fund (Business funds). The DBMS accounted for general funds to a significantly lesser degree than the Business funds. DFAS, Headquarters, personnel stated that subsidiary ledgers are reconciled to general ledger accounts and that the needed audit trails exist, under DBMS, for the Business Funds.

The DFAS did not identify the need to reconcile proprietary with budgetary general ledger accounts as an assessable unit. However, the DFAS-Columbus Center was drafting an instruction, specifying the need to reconcile proprietary and budgetary general ledger accounts. The DFAS-Columbus Center was also holding classes on the DBMS trial balance process, which emphasized the need to reconcile proprietary with budgetary general ledger accounts to help ensure reliable financial information.

Other Reviews

During the last five years, the DFAS Richmond Detachment was the only activity that issued a report on the DLA general funds.

The DFAS Richmond Detachment report, "Evaluation of the Appropriated Accounting Sub-System of the Defense Business Management System (DBMS) at the Defense Finance and Accounting Service, Columbus Center, Columbus, Ohio," April 15, 1994, reported that internal controls in the vendor payment area were insufficient. The report also stated that additional training was required, large backlogs existed in some areas, no single source of data entry existed, the DBMS did not use a standard general ledger, DFAS-Columbus Center expended a great deal of resources to manually record data in DBMS, and reconciliations were not consistently performed to ensure accurate financial data. The report made 13 recommendations (10 to the DFAS-Columbus Center and 3 to DFAS, Headquarters) specifically related to reconciliation weaknesses. The 13 recommendations stated either that specific reconciliations should be performed or that accounting system change requests should be developed so that reconciliations could be more readily performed.

Appendix A. Audit Process

The DFAS concurred with 12 of the 13 recommendations. It nonconcurred with the recommendation to provide support for obligated amounts because DFAS stated that the report cited an obligation that was not a DFAS-Columbus Center transaction.

Although DFAS stated that corrective actions would be completed by June 1994, as of May 1996, some of the same reconciliation weaknesses that the DFAS Richmond Detachment reported still existed.

Appendix B. Defense Logistics Agency FY 1995 General Funds

<u>Fund Source</u>	<u>Appropriation Code</u>	<u>Funds Received</u>	<u>Percent of Total</u>
Operation and Maintenance	9750100.51	\$1,568,213,000	82
Operation and Maintenance	9750100.6101	94,084,000	5
Research and Development	9750400.51	129,352,000	7
Base Realignment and Closure	97X0510.16A6	71,700,000	4
Military Construction	9750500.51	17,764,000	1
Procurement Defense Wide	9750300.51	17,587,000	1
Humanitarian Assistance	974/50819.2051	2,490,000	
Humanitarian Assistance	9750891.2051	1,500,000	
Family Housing Operation and Maintenance	9750706.51	<u>1,488,000</u>	
Total		\$1,904,178,000	

Appendix C. Imbalances Between General Ledger and Subsidiary Ledgers

We reviewed the DBMS central data base because it was the single largest data base applicable to the DLA Operation and Maintenance appropriation. The central data base contained \$580 million (34 percent) of the DLA \$1.7 billion funding for Operation and Maintenance. We identified general and subsidiary ledger imbalances totaling \$543 million.

<u>Types of Accounts</u>	<u>General Ledger</u>	<u>Subsidiary Ledgers</u>	<u>Imbalance</u>
Receivables	\$ 96,604,326 ¹	\$ 65,111,786 ²	\$ 31,492,540
Expenses	671,213,464 ¹	159,507,376 ³	<u>511,706,088⁴</u>
Total			\$543,198,628

¹General ledger receivables and expenses were obtained from the UPFE600A and UPFE650A trial balances at September 30, 1995, for the DBMS central data base.

²Subsidiary ledger receivables were obtained from the September 30, 1995, UPFE200A subsidiary ledgers for the DBMS central data base.

³Subsidiary ledger expenses were obtained from the September 30, 1995, UPCE300B subsidiary ledgers for the DBMS central data base.

⁴According to DFAS-Columbus Center personnel, this difference existed because the subsidiary ledgers did not include expenses from prior years.

Appendix D. Imbalances Between Proprietary and Budgetary Equivalents

<u>Accounts Involved</u>	<u>Proprietary</u>		<u>Budgetary</u>	<u>Imbalance</u>
Cash Account Equivalents	Undistributed Disbursements GLAC* 111.000	=	Undistributed Disbursements GLAC 471.000	\$641,884,251
	Undistributed Collections GLAC 112.000	=	Undistributed Collections GLAC 472.000	141,913,502
Receivable Account Equivalents	Accounts Receivable GLAC 121.000	=	Operating Reimbursements Earned - Uncollected GLAC 455.000 +	6,427,896
			Restricted Reimbursements Earned - Uncollected GLAC 462.000	
Accrued Payable and Liabilities Account Equivalents	Accounts & Claims Payable GLAC 210.000 +	=	Accrued Expenditures - Unpaid GLAC 410.000	8,759,947
	Accrued Liabilities GLAC 220.000			
Revenue Account Equivalents	Reimbursable Sales GLAC 510.100	=	Cumulative Operating Reimbursements Earned GLAC 457.000 +	48,026,588
			Cumulative Restricted Reimbursements Earned GLAC 464.000 (FY 1995 only)	
Operating Expenses Equivalents	Operating Expenses GLAC 610.000 +	=	Accrued Expenditures GLAC 413.000	47,435,505
	Refunds Receivable GLAC 123.000(change)		(FY 1995 only)	
Total				\$894,447,689

* General Ledger Account.

Appendix E. Supporting Documentation for Accounts Receivables Selected From the Receivables Subsidiary Ledger

Four document numbers were selected from the DBMS central database receivables subsidiary ledger ending September 30, 1995. The transaction histories for these four document numbers were not available.

<u>Document Number</u>	<u>Amount</u>	<u>Date</u>
9501PURG06765	\$ 22,743	December 31, 1994
9501PURG02039	51,103	December 31, 1994
91DFSC1	13,807,210	September 30, 1991
91SF	<u>3,744,620</u>	September 28, 1991
Total	\$17,625,676	

The four documents shown above represent 27 percent of the \$65 million in the DBMS central database subsidiary ledger for receivables.

Appendix F. 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
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
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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

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Part III - Management Comments

Defense Finance and Accounting Service Comments



DEFENSE FINANCE AND ACCOUNTING SERVICE

1931 JEFFERSON DAVIS HIGHWAY
ARLINGTON, VA 22240-5291

NOV - 6 1996

DFAS-HQ/AFB

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

SUBJECT: Revised Management Comments on the DoD IG Draft
Report, "General Fund Trial Balance of the Defense
Logistics Agency at September 30, 1995" (Project
No. 6LA-2005.01)

As a result of the October 16, 1996, meeting between
your staff and our Columbus Center staff, our revised
management comments are attached.

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

A handwritten signature in dark ink, appearing to read "Tm".

Thomas F. McCarty
Deputy Director for
Accounting

Attachment

Defense Finance and Accounting Service Comments

RECOMMENDATION 1: We recommend that the Commander, Defense Finance and Accounting Service-Columbus Center accelerate the implementation of accounting system changes to readily allow identification of account imbalances and to provide the needed audit trail to correct identified imbalances.

Management comments: Concur. It is anticipated that the segregation of non-Defense Business Operations Fund proprietary accounts will take place in the third quarter of fiscal year 1997 through Defense Business Management System (DBMS) release 9.000, as part of the System Change Request implementing the conversion to the DoD Standard General Ledger. Any benefit that could be derived from acceleration would only be realized if the change is fielded prior to September 30, 1996. As of August 15, 1996, only high-level requirements have been identified for this change. It would be virtually impossible to define detail requirements, perform the necessary coding and Central Design Activity and User testing, and field this change within 6 weeks. In addition, we believe that researching and correcting the remaining out-of-balance conditions are necessary prior to converting the accounts to the level suggested in the recommendation. If these balances are not corrected, then the values established at the time of conversation would be suspect.

Estimated Completion Date: July 31, 1997.

RECOMMENDATION 2: We recommend that the Commander, Defense Finance and Accounting Service-Columbus Center reconcile accounts so that the Defense Logistics Agency FY 1996 financial statements can be more reliable.

Management comments: Concur. The Defense Finance and Accounting Service - Columbus Center Accounting Directorate (DFAS-CO-A) currently performs multiple reconciliations focused on the resolution of abnormal balances and correction of out-of-balance conditions between general ledger and subsidiary accounts. As part of this ongoing effort to reconcile account balances, DFAS-CO-A is continuing to look for ways to enhance the current reconciliation process. We will implement any tools that will allow our accounts to improve the current process.

Estimated Completion Date: October 31, 1996.

Defense Finance and Accounting Service Comments

Additional management comments: These management comments are the result of a meeting on October 16, 1996, among representatives of the Department of Defense Inspector General (DoDIG); the Defense Finance and Accounting Service - Columbus Center (DFAS-CO), Internal Review Office; the DFAS-CO Defense Business Management Systems (DBMS) Project Management Office; and the DFAS-CO Directorate of Accounting to discuss the "Additional Management Comments" included in the DFAS-HQ/AFB memorandum of September 10, 1996, to the DoDIG in response to the subject draft audit report.

DFAS-CO recognizes that out-of-balance conditions exist between the proprietary and budgetary accounts for the Defense Logistics Agency (DLA) General Funds. The DoDIG analysis indicates that a \$894.4 million imbalance exists between the budgetary and proprietary accounts. On the other hand, DFAS-CO determined that the imbalance is \$309.6 million. The methodology used by the DoDIG to compute the difference is based on absolute values, e.g., compute the difference between the proprietary and budgetary accounts in one subhead, perform the same calculation for the other subhead, and then add the two differences to arrive at an absolute difference. DFAS-CO used a different approach which netted the difference, e.g., if the difference between the GLAC's in one subhead resulted in a +200,000 and the difference in the other subhead was -100,000, the net difference is +100,000. The DoDIG absolute difference in this example would be +300,000. The major effect the different methodologies have is on the materiality of the variance. Regardless of which methodology is the appropriate one for presentation purposes, DFAS-CO is committed to correcting the root cause of these problems as outlined below.

DFAS-CO is researching the cause of the variance and working to resolve it. DFAS-CO is attempting to determine why the proprietary accounts are being updated under two different DLA subheads. DBMS, as it currently exists, should be updating all General Funds proprietary balances for DLA by basic symbol under subhead 5110 only. DFAS-CO will work with the DFAS Financial Systems Activity Columbus to identify the cause of the problem.

Estimated Completion Date: September 30, 1997.

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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INTERNET DOCUMENT INFORMATION FORM

A . Report Title: General Fund Trial Balance of the Defense Logistics Agency at September 30, 1995

B. DATE Report Downloaded From the Internet: 11/03/99

C. Report's Point of Contact: (Name, Organization, Address, Office Symbol, & Ph #): OAIG-AUD (ATTN: AFTS Audit Suggestions)
Inspector General, Department of Defense
400 Army Navy Drive (Room 801)
Arlington, VA 22202-2884

D. Currently Applicable Classification Level: Unclassified

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