

Inspector General

United States
Department of Defense



Internal Controls Over the United States Marine Corps
Military Equipment Baseline Valuation Effort

Report Documentation Page

Form Approved
OMB No. 0704-0188

Public reporting burden for the collection of information is estimated to average 1 hour per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing this burden, to Washington Headquarters Services, Directorate for Information Operations and Reports, 1215 Jefferson Davis Highway, Suite 1204, Arlington VA 22202-4302. Respondents should be aware that notwithstanding any other provision of law, no person shall be subject to a penalty for failing to comply with a collection of information if it does not display a currently valid OMB control number.

1. REPORT DATE 09 FEB 2009	2. REPORT TYPE	3. DATES COVERED 00-00-2009 to 00-00-2009			
4. TITLE AND SUBTITLE Internal Controls Over the United States Marine Corps Military Equipment Baseline Valuation Effort		5a. CONTRACT NUMBER			
		5b. GRANT NUMBER			
		5c. PROGRAM ELEMENT NUMBER			
6. AUTHOR(S)		5d. PROJECT NUMBER			
		5e. TASK NUMBER			
		5f. WORK UNIT NUMBER			
7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES) Department of Defense Inspector General, ODIG-AUD, 400 Army Navy Drive, Arlington, VA, 22202-4704		8. PERFORMING ORGANIZATION REPORT NUMBER			
9. SPONSORING/MONITORING AGENCY NAME(S) AND ADDRESS(ES)		10. SPONSOR/MONITOR'S ACRONYM(S)			
		11. SPONSOR/MONITOR'S REPORT NUMBER(S)			
12. DISTRIBUTION/AVAILABILITY STATEMENT Approved for public release; distribution unlimited					
13. SUPPLEMENTARY NOTES					
14. ABSTRACT					
15. SUBJECT TERMS					
16. SECURITY CLASSIFICATION OF:			17. LIMITATION OF ABSTRACT Same as Report (SAR)	18. NUMBER OF PAGES 30	19a. NAME OF RESPONSIBLE PERSON
a. REPORT unclassified	b. ABSTRACT unclassified	c. THIS PAGE unclassified			

Additional Information and Copies

To obtain additional copies of this report, visit the Web site of the Department of Defense Inspector General at <http://www.dodig.mil/audit/reports> or contact the Secondary Reports Distribution Unit at (703) 604-8937 (DSN 664-8937) or fax (703) 604-8932.

Suggestions for Audits

To suggest ideas for or to request future audits, contact the Office of the Deputy Inspector General for Auditing at (703) 604-9142 (DSN 664-9142) or fax (703) 604-8932. Ideas and requests can also be mailed to:

ODIG-AUD (ATTN: Audit Suggestions)
Department of Defense Inspector General
400 Army Navy Drive (Room 801)
Arlington, VA 22202-4704

DEPARTMENT OF DEFENSE

hotline

To report fraud, waste, mismanagement, and abuse of authority.

Send written complaints to: Defense Hotline, The Pentagon, Washington, DC 20301-1900
Phone: 800.424.9098 e-mail: hotline@dodig.mil www.dodig.mil/hotline

Acronyms and Abbreviations

MARCORSYSCOM	Marine Corps Systems Command
P&EPO	Property and Equipment Policy Office
PMO	Program Management Office
PPS	Proportional to Size
SFFAS	Statement of Federal Financial Accounting Standards
USMC	United States Marine Corps



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

February 9, 2009

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

SUBJECT: Internal Controls Over the United States Marine Corps Military Equipment
Baseline Valuation Effort (Report No. D-2009-049)

We are providing this report for review and comment. We considered comments from the United States Marine Corps on a draft when preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The United States Marine Corps comments were nonresponsive to Recommendations 1 and 2, but partially responsive to Recommendation 3. We request additional comments on Recommendations 1, 2, and 3. Therefore, we request that the Commandant, United States Marine Corps provide comments by March 9, 2009. See the recommendations table on page ii.

Please provide comments that conform to the requirements of DoD Directive 7650.3. If possible, send client comments in electronic format (Adobe Acrobat file only) to AudDBO@dodig.mil. Copies of the client comments must have the actual signature of the authorizing official for your organization. We cannot accept the / Signed / symbol in place of the actual signature. If you arrange to send classified comments electronically, you must send them over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 601-5868 (DSN 329-5868).

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



Results in Brief: Internal Controls Over the United States Marine Corps Military Equipment Baseline Valuation Effort

What We Did

The Property and Equipment Policy Office (P&EPO) in the Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics requested that the DoD Office of Inspector General perform procedures to review the military equipment baseline valuation as of September 30, 2006. Officials from both offices discussed and agreed upon objectives for the audit, which included evaluating the reliability of the internal controls over three of the financial statement assertions: valuation, rights and obligations, and completeness. We assessed the effectiveness of the P&EPO and United States Marine Corps (USMC) internal controls over the valuation, rights and obligations, and completeness of military equipment programs. We reviewed the P&EPO packages and supporting documentation. We compared a Capital Asset Management System-Military Equipment list to budget and accounting system reports provided as support. We judgmentally selected programs that had received waivers issued by the Property and Equipment Policy Office to determine whether the waivers were adequately supported. This report is one in a series. The final report will summarize all findings for the series and recommend corrective actions, as appropriate.

What We Found

P&EPO and USMC did not have adequate controls in place over the USMC military equipment baseline. As a result, USMC:

- valuation, rights and obligations, and completeness assertions were unsupported;

- military equipment valuation had \$2.1 billion, of \$5.9 billion, in unsupported acquisition costs and a potential \$12 million understatement in the valuation as of September 30, 2006; and
- military equipment programs had 116 unsupported waivers of 148 judgmentally selected waivers.

What We Recommend

We recommend that the Commander of the Marine Corps Systems Command and Program Executive Officer for Land Systems ensure that:

- program managers maintain supporting documentation for valuations, waivers, useful lives, and program completeness and
- all waivers meet the definition of military equipment waivers and are monitored for changes in waiver status.

Client Comments and Our Response

The Commandant of the United States Marine Corps disagreed with two recommendations, but agreed with one recommendation. His comments were not fully responsive and we request that the Commandant, United States Marine Corps provide additional comments by March 9, 2009. Please see the recommendations table on the back of this page. Please see the finding section of the report for a detailed discussion of the agency comments and our response.

Recommendations Table

Client	Recommendations Requiring Comment	No Additional Comments Required
Commandant, United States Marine Corps	1, 2, and 3	

Please provide comments by March 9, 2009.

Table of Contents

Results in Brief	i
Introduction	
Objectives	1
Background	1
Review of Internal Controls	3
Management Assertions	3
Finding. United States Marine Corps Military Equipment Baseline	5
Client Comments on the Finding and Our Response	8
Recommendations, Client Comments, and Our Response	9
Appendices	
A. Scope and Methodology	13
Prior Coverage	14
B. Statistical Sampling Methodology	15
Client Comments	
United States Marine Corps	17

Introduction

Objectives

Our objective was to determine whether internal controls over the valuation of the United States Marine Corps (USMC) military equipment baseline were adequate. Specifically, we assessed the effectiveness of the Property and Equipment Policy Office (P&EPO) and USMC internal controls over the valuation, rights and obligations, and completeness of military equipment programs. See Appendix A for a discussion of the scope and methodology and for prior coverage related to the objectives.

Background

The P&EPO in the Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics requested that the DoD Office of Inspector General perform procedures to review the military equipment baseline as of September 30, 2006. Officials in the P&EPO and the Office of Inspector General discussed and agreed upon objectives for this audit. The agreed-upon objectives included evaluating the reliability of the internal controls over the financial statement assertions: valuation, rights and obligations, and completeness of military equipment programs.

The Under Secretary of Defense for Acquisition, Technology, and Logistics and the Under Secretary of Defense (Comptroller)/DoD Chief Financial Officer established the P&EPO in December 2000 to ensure a consistent military equipment valuation methodology. The P&EPO led the Department-wide effort to achieve compliance with Statement of Federal Financial Accounting Standards (SFFAS) No. 23, “Eliminating the Category National Defense Property, Plant, and Equipment,” by developing the military equipment program universe and performing the initial military equipment valuation. The P&EPO developed the universe to identify all military equipment programs. The P&EPO used budget reports and asset data obtained from DoD accountability and logistics systems to develop the military equipment program universe. The initial military equipment valuation developed a value for the military equipment programs for inclusion in the DoD financial statements. The process was a manual effort that began in FY 2002 and continued through FY 2006 with the implementation of Capital Asset Management System-Military Equipment. The Capital Asset Management System-Military Equipment captures asset status and expenditures. In addition, it values, capitalizes, and depreciates delivered assets, and it reports financial and management data.

Military equipment valuation is a DoD-wide effort to implement Federal accounting standards requiring military equipment to be capitalized and recorded on the DoD financial statements. Previously, DoD classified military equipment as National Defense Property, Plant, and Equipment, which was expensed in the year it was acquired. In May 2003, the Federal Accounting Standards Advisory Board issued SFFAS No. 23, which eliminated the category of National Defense Property, Plant, and Equipment and

reclassified military equipment as General Property, Plant, and Equipment. SFFAS No. 23 requires that the initial capitalization amount for assets previously considered National Defense Property, Plant, and Equipment be based on historical cost in accordance with the asset recognition provisions of SFFAS No. 6, "Accounting for Property, Plant and Equipment," as amended and should be the initial historical cost for the items, including any major improvements or modifications.

SFFAS No. 6 defines Property, Plant, and Equipment as tangible assets that have an estimated useful life of 2 or more years, are not intended for sale in the ordinary course of business, and are intended to be used or available for use by the entity. SFFAS No. 6 states that depreciation expense is calculated through the systematic and rational allocation of the cost of General Property, Plant, and Equipment, less its estimated salvage or residual value, over the estimated useful life of the General Property, Plant, and Equipment. The Standard requires costs that extend the useful life of existing General Property, Plant, and Equipment or increase or improve its capacity to be capitalized and depreciated and/or amortized over the remaining useful life of the associated General Property, Plant, and Equipment.

DoD Regulation 7000.14-R, the "DoD Financial Management Regulation," volume 4, chapter 6, "Property, Plant, and Equipment," July 2006, defines General Property, Plant, and Equipment as tangible assets that meet all of the following criteria:

- have an estimated useful life of 2 years or more;
- are not intended for sale in the ordinary course of operations;
- are acquired or constructed with the intention of being used or available for use by the entity; and
- have an initial acquisition cost, book value or, when applicable, an estimated fair market value that equals or exceeds the DoD capitalization threshold, which is \$100,000.

This includes assets that had previously been classified as National Defense Property, Plant, and Equipment; bulk purchases; and assets used in providing goods or services. It also includes assets that support the mission of the entity. Additionally, the costs to improve General Property, Plant, and Equipment should be capitalized when the improvement increases the asset's capability, size, efficiency, and useful life, or modifies functionality and would not otherwise be considered maintenance or repairs.

All General Property, Plant, and Equipment assets acquired by DoD must be recognized for accountability and financial reporting purposes. Recognition requires the proper accounting treatment (expense or capitalization and depreciation or amortization) and the reporting of capitalized amounts and accumulated depreciation or amortization on the appropriate DoD Component's financial statements. The DoD Component that procures a General Property, Plant, and Equipment asset or the DoD Component in possession of a

General Property, Plant, and Equipment asset will be the DoD Component that accounts for and reports the asset.¹

Review of Internal Controls

We determined that material internal control weaknesses, as defined by DoD Instruction 5010.40, “Managers’ Internal Control (MIC) Program Procedures,” January 4, 2006, existed in the military equipment valuation processes. DoD Instruction 5010.40 states that internal controls are the organization, policies, and procedures that help program financial managers to achieve results and safeguard the integrity of their programs. The P&EPO and USMC military equipment PMOs did not maintain adequate controls to ensure that documents supporting valuations, rights and obligations, and completeness of its military equipment programs were obtained, retained and available for audit. Implementing the recommendations will improve the controls over the military equipment valuation processes and support for the valuation, rights and obligation, and completeness assertions for military equipment programs. Although we identified material weaknesses in the P&EPO process for valuing military equipment, we are making no recommendations to the P&EPO to correct them in this report. This report is one in a series and the final report will summarize all findings in the series and recommend corrective actions for the P&EPO internal control weaknesses. A copy of the final report will be provided to the senior officials in charge of management controls.

Management Assertions

Management assertions are representations by management about information in the financial statements. The primary management assertions for the Military Equipment line item are listed in Table 1.

Table 1. Management Assertions	
<u>Assertion</u>	<u>Management Representation</u>
Valuation or Allocation	All military equipment is properly valued.
Rights and Obligations	The USMC owns all military equipment reported in the financial statements.
Completeness	All military equipment owned by the USMC is reported in the financial statements.
Existence or Occurrence	All military equipment assets reported in the financial statements existed at the time.
Presentation and Disclosure	All military equipment assets are correctly reported in the financial statements.

Our audit focused on the assertions for valuation, rights and obligations, and completeness of program universe applicable to the USMC military equipment baseline.

¹ The DoD Regulation 7000.14-R also refers to this principle as the preponderance of use.

Finding. United States Marine Corps Military Equipment Baseline

The internal controls over the United States Marine Corps (USMC) military equipment baseline were inadequate. Specifically, the USMC military equipment program valuation, rights and obligations, and completeness of universe program assertions as of September 30, 2006, were not sufficiently supported because the Property and Equipment Policy Office (P&EPO) and USMC did not have adequate internal controls over the processes for obtaining and maintaining supporting documentation. As a result, USMC could not support \$2.1 billion out of a sample of \$5.9 billion in military equipment costs. In addition, the USMC military equipment baseline could be misstated by an additional \$12 million that was not included in the baseline. Finally, military equipment programs that were identified as waived programs were not adequately supported, and the USMC's rights and obligations pertaining to 14 military equipment programs could not be verified. Without positive assurance regarding the valuation, rights and obligations, and completeness of financial statement assertions, the potential for a material financial statement misstatement exists.

Valuation Assertion

P&EPO and USMC internal controls did not ensure that valuations were based on appropriate documentation and methodologies. Proper valuation, which includes accumulated depreciation, must be supported by acquisition cost, the date of acquisition or placed-in-service date, and useful lives of the assets. USMC could not support its military equipment baseline valuation as of September 30, 2006. The P&EPO provided valuation packages that were supposed to contain an executive summary, the valuation model, completed questionnaires provided by program managers, and available supporting documentation provided by the program managers. P&EPO personnel provided training to USMC program managers on maintaining support for the historical cost baseline packages for each program because auditors and others would be requesting that information. However, USMC could not provide the required support for these questionnaires and, ultimately, the baseline valuation.

Budget documents and other types of documentation are acceptable supporting documentation for military equipment if obtaining initial historical cost is not practical. The P&EPO and USMC provided accounting system reports and budget documents to support reported acquisition costs for assets. The USMC military equipment programs were valued at \$7.3 billion as of September 30, 2006. We selected a sample of 14² of 64 military equipment programs for review. The programs represented \$5.9 billion or

² For the 14 programs selected, we combined the original acquisition and its associated modifications into one program resulting in 13 programs reviewed.

81 percent of the reported acquisition value. The P&EPO and USMC provided insufficient supporting documentation for \$2.1 billion of \$5.9 billion of the programs selected for review. The Material Handling Equipment program could be misstated by an additional \$12 million that was adequately supported but was not included in the baseline. The remaining program valuation costs were adequately supported. Table 2 shows the reported military equipment values as of September 30, 2006, for the individual programs in our sample and the respective acquisition costs that USMC was not able to adequately support.

Table 2. Reported Military Equipment Value at September 30, 2006, for Programs Reviewed³ (in millions)		
Military Equipment Program	Acquisition Cost Reviewed	Unsupported Acquisition Cost Reviewed
Advanced Amphibious Assault Vehicle- Product Improvement Plan	\$ 466.5	\$ 8.5
AN TQP 36/46 Firefinder Radar	39.0	2.2
Cougar, Mine Protected Armored Protection Patrol Vehicle	78.4	54.6
High Mobility Multi-Purpose Wheeled Vehicle	1,310.5	497.6
Javelin Command Launch Unit	334.1	215.9
Joint Surveillance Target Attack Radar System	13.4	4.7
Light Armored Vehicle	776.1	20.3
Lightweight 155mm Howitzer	195.0	58.0
M1A1 Abrams Main Battle Tank	801.8	801.8
Marine Corps Air Ground Combat Center	60.4	21.0
Material Handling Equipment	293.2	70.3
Medium Tactical Vehicle Replacement	1,315.2	178.3
Visual Information Systems	<u>207.9</u>	<u>199.1</u>
Total	\$5,891.5	\$2,132.3

For our sampled programs, we compared the Capital Asset Management System-Military Equipment to completed questionnaires, budget reports, and accounting system reports. USMC program management offices (PMOs) referred to only the P&EPO valuation packages as supporting documentation. These valuation packages did not contain supporting documentation to support acquisition date, date of receipt, or useful lives. The insufficient support for useful lives was also identified in the P&EPO, Office of Under Secretary of Defense for Acquisition, Technology, and Logistics, “Internal Validation and Verification Project, Military Equipment Valuation,” report, June 13, 2006.

³ Our review was performed at the program level and not at the end-item or unit level because the P&EPO and USMC could not provide supporting documentation.

During our review of the 13 USMC military equipment programs, we identified different baseline valuation support problems for each program. For example, for the Advanced Amphibious Assault Vehicle-Product Improvement Plan and Lightweight 155mm Howitzer military equipment programs, P&EPO and USMC personnel calculated the program valuations using expected units purchased and expected expenditures instead of current units purchased and current expenditures. For the Javelin Command Launch Unit, the program included ordinance in the total program valuation, but USMC personnel did not provide supporting documentation that confirmed how much of the program was for ordinance. Finally, USMC personnel did not provide any supporting documentation for the M1A1 Abrams Main Battle Tanks. USMC did not provide any additional documentation to support the military equipment baseline valuation; therefore, we cannot determine whether amounts reported for acquisition costs, depreciation, accumulated depreciation, or the resulting net book value of military equipment were supported.

Rights and Obligations Assertion

USMC could not provide supporting documentation that proved that USMC owned the military equipment in its baseline as of September 30, 2006. DoD provides guidance for verifying rights and obligations using:

- valid receipt and acceptance documentation, for example, DD250s;
- contract documents after fiscal year 2002 (which is mandated by SFFAS No. 23); and
- written directives detailing the preponderant use of assets.

USMC did not adequately support its rights and obligations. USMC provided questionnaires, but they did not provide the documentation supporting questionnaire responses. We requested the USMC PMOs provide:

- access to PMO personnel for the purposes of conducting interviews and obtaining supporting documentation and background information about where they keep supporting documentation,
- receiving documents, and
- engineering studies to support useful lives and depreciation calculations.

The USMC PMOs were unable to provide the requested documentation. Therefore, we cannot determine whether the rights and obligations assertion for USMC military equipment programs is accurate.

Completeness Assertion

The military equipment valuation methodology allowed certain military programs to receive waivers from valuation, which DoD granted. We reviewed the following types of waivers.

- Temporary waivers issued for programs using research and development funding that did not require valuation at the time of assessment, but were expected to receive procurement funding in the future. They were to be reassessed annually.
- Software waivers issued for software integrated into weapons systems. The software was capitalized as part of the cost of the related military equipment program.
- Price waivers issued for assets that did not meet capitalization thresholds for military equipment.

USMC could not provide sufficient supporting documentation to allow an independent assessment of 116 of the 148 sampled military equipment waivers. Without verifying the validity of the waivers, P&EPO and USMC could not ensure that the military equipment valuation baseline included all valid programs and excluded all allowable waived programs. Further, depending on the validity of the waiver, the military equipment valuation on the financial statements could be misstated.

We reviewed 23 temporary waivers, 20 software waivers, and 105 price waivers as of September 30, 2006, to determine whether the waivers were adequately supported. For the temporary waivers, USMC did not support that the equipment was still in research and development. USMC did not adequately explain why it valued software operating within military equipment separately as internal use software. This type of software normally would be valued and reported as military equipment. For the price waivers, USMC did not document that the cost of the items was less than \$100,000. USMC did not fully support waived USMC programs. Therefore, the completeness of USMC military equipment programs may be inaccurate. These inaccuracies will also directly impact program valuations.

Client Comments on the Finding and Our Response

The Commandant, United States Marine Corps comments on the finding did not specifically address the finding. The comments provided were in relation to each of the recommendations. Please see the following section for his comments and our response.

Recommendations, Client Comments, and Our Response

We recommend that the Commandant, United States Marine Corps ensure that program managers:

1. Maintain required documentation to support military equipment valuations, acquisition and disposal dates, useful lives, waivers, and program completeness.

USMC Comments

The Commandant, United States Marine Corps disagreed. He stated that maintaining supporting documentation was a P&EPO responsibility. The United States Marine Corps followed the Office of the Secretary of Defense P&EPO guidance for establishing the initial valuation of all known military equipment programs. Marine Corps Systems Command (MARCORSYSCOM) program managers completed the questionnaires for the programs identified by the P&EPO. The P&EPO-approved questionnaires should serve as acceptable documentation for the inventory value as of September 30, 2006. Since FY 2007, the United States Marine Corps records asset additions, disposals, and transfers in Capital Asset Management System-Military Equipment; and MARCORSYSCOM maintains supporting documentation for military equipment valuation. MARCORSYSCOM can be accountable for the source documentation it provided to populate Capital Asset Management System-Military Equipment, but it cannot be accountable for the information produced after that point.

Our Response

The Commandant, United States Marine Corps comments were nonresponsive. The P&EPO provided training to USMC Components logistics and acquisitions personnel on the audit documentation requirements for the military equipment baseline. The P&EPO is a support office established to help address military equipment valuation and accountability issues from a DoD-wide perspective. The P&EPO training documentation specifically stated what information would need to be maintained for audit purposes. For example, the training documentation stated that the United States Marine Corps must maintain original source documentation, such as contract records, delivery receipt documentation, and payment records necessary to support the various valuation aspects of military equipment. The guidance issued by the P&EPO never intended for the questionnaires to serve as the sole support for military equipment valuation as of September 30, 2006. Consequently, the P&EPO-approved questionnaires are not considered adequate supporting documentation for the military equipment baseline. In addition, it is the United States Marine Corps' responsibility to support the amounts stated on their financial statements regardless of the support provided by the P&EPO.

Although the United States Marine Corps began maintaining military equipment supporting documentation in FY 2007, this does not apply to the supportability of the military equipment baseline as of FY 2006. The stated objective of this audit was to

assess the effectiveness of internal controls over the validation, rights and obligations, and completeness of military equipment programs. The United States Marine Corps did not demonstrate that adequate internal controls were in place over the United States Marine Corps military equipment baseline valuation because it could not support these valuations with appropriate source documentation as required by P&EPO guidance and accounting standards.

We request that the Commandant, United States Marine Corps ensure that program managers maintain required documentation to support military equipment valuations, acquisitions and disposal dates, useful lives, waivers, and program completeness. We also request that the Commandant, United States Marine Corps reconsider his position on the recommendation and provide comments on the final report.

2. Review waived programs as required and maintain documentation to support the military equipment waiver status.

USMC Comments

The Commandant, United States Marine Corps disagreed with the recommendation. He stated that this is a P&EPO responsibility.

Our Response

The Commandant, United States Marine Corps comments were nonresponsive. The United States Marine Corps program managers are responsible for reviewing waived programs and maintaining supporting documentation to support the waiver status. The program managers, with assistance from the P&EPO valuation teams, determined if military equipment programs should be waived. The P&EPO personnel discussed criteria for waivers with program managers. The P&EPO Management Assertion Package, Tab 1 stated:

- (1) temporary waivers were to be reassessed annually by program managers;
- (2) software waivers were only to be issued for software integrated into weapons systems;
- and (3) price waivers were to be granted for assets that don't meet the capitalization threshold for military equipment.

The program managers did not submit supporting documentation for the signed waiver letters. The program managers should have documentation to support why they signed the waiver letters.

We request that the Commandant, United States Marine Corps ensure that program managers review and maintain documentation to support the military equipment waiver status. We also request that the Commandant, United States Marine Corps reconsider his position on the recommendation and provide comments on the final report.

3. Implement the management controls established by Property and Equipment Policy Office, Acquisition, Technology, and Logistics and United States Marine Corps Headquarters policy statements, directives, and regulations.

USMC Comments

The Commandant, United States Marine Corps agreed with this recommendation. The Commander, Marine Corps Systems Command has implemented controls to support all asset information provided to P&EPO.

Our Response

The Commandant, United States Marine Corps comments were partially responsive. The Commandant, United States Marine Corps did not identify the implemented actions and completion dates for the implemented controls to support all asset information provided to P&EPO. We request that the Commandant, United States Marine Corps provide comments in response to the final report that explain the management controls implemented and provide the associated implementation dates.

Appendix A. Scope and Methodology

We conducted this financial-related audit from July 2007 through March 2008 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objectives for this audit were to evaluate the reliability of the internal controls over three of the financial statement assertions: valuation, rights and obligations, and completeness of the military equipment program universe. We reviewed the reasonableness and reliability of the estimated historical acquisition cost that USMC developed using the documentation provided by the P&EPO from the valuation effort conducted by KPMG. KPMG was contracted with to develop an auditable historic baseline and related documentation packages that met all audit requirements. The documents reviewed included budget documents and reports from the Standard Accounting, Budgeting, and Reporting System financial reports. The PMOs that responded to our requests stated they previously provided all support for the baseline values to KPMG. The PMOs provided no additional support information.

We statistically selected and reviewed 14 of 64 military equipment acquisition and modification programs. We combined one program and its associated modifications under one program resulting in 13 programs reviewed. In addition, we judgmentally selected 148 waived USMC military equipment programs. The review was not intended to address the existence of the assets represented by reported program values.

Use of Computer-Processed Data

We relied on computer-processed data provided directly from P&EPO and its support contractor. Specifically, we used the computer-processed data to review program valuation calculations and examine supporting documentation adequacy. We did not determine the reliability of computer-processed data. Not evaluating the controls did not affect the results of the applications of the agreed-upon procedures.

Use of Technical Assistance

The DoD IG Quantitative Methods Directorate assisted with the audit. See Appendix B for detailed information about the work performed by the Quantitative Methods Directorate.

Prior Coverage

During the last 5 years, the Department of Defense Inspector General (DoD IG) has issued two reports related to military equipment. Unrestricted DoD IG reports are available at <http://www.dodig.mil/audit/reports>.

DoD IG

DoD IG Report No. D-2005-112, “Report on Review of the Development of the DoD Baseline for Military Equipment,” September 30, 2005

DoD IG Report No. D-2005-114, “Report on Review of the DoD Baseline for Military Equipment,” September 30, 2005

Appendix B. Statistical Sampling Methodology

Quantitative Plan

Objective: To determine whether acquisition valuations were correct and if control procedures were correctly followed.

Population: The population consisted of an Excel file containing 64 programs valued at \$7,296,753,356 and contained 20,032 end item transactions. The programs were categorized by average cost and group composite method. There were 44 programs using an average cost method that amounted to \$3,422,707,271 that contain 19,912 end item transactions. There were 20 programs using a group composite method that amounted to \$3,874,046,085 that contained 120 end items.

Measures: The variable measure was the dollar difference between the stated item value and the audited value. The attribute measure of correct or incorrect was used to determine if the item audited met the required conditions.

Parameters: We used a 90 percent confidence level for the statistical estimate.

Sample Plan

We used a two-stage sample design. Stage 1 was a probability proportional to size (pps) design by acquisition value. Stage 2 was a simple random sample of program end items. Programs were sampled separately based on the costing method, average cost, and group composite.

Stage 1 average cost. We selected 15 programs using pps with replacement. We selected nine unique programs.

Stage 1 group composite. We selected 15 programs using pps with replacement. We selected 5 unique programs.

Stage 2 average cost. We randomly selected 10 end items from each of the 15 average cost programs without replacement. Total sample size was 288.

Stage 2 group composite. We randomly selected 20 end items from each of the 15 group composite programs without replacement. If there were fewer than 20 end items in a program, we selected 100 percent of the items. Total sample size was 115. We used the random number generator in SAS version 9.1 to select the random samples.

Statistical Analysis and Interpretation

USMC did not provide sufficient supporting documentation for the valuation of the programs selected for review. Therefore, Quantitative Methods Directorate did not make any statistical projections.

United States Marine Corps Comments



DEPARTMENT OF THE NAVY
HEADQUARTERS UNITED STATES MARINE CORPS
3000 MARINE CORPS PENTAGON
WASHINGTON, DC 20350-3000

IN REPLY REFER TO:
7FN-0216
RFR-80
8 Oct 08

MEMORANDUM FOR DEPARTMENT OF DEFENSE OFFICE OF THE DEPUTY
INSPECTOR GENERAL FOR AUDITING, DEFENSE FINANCIAL
AUDITING SERVICE

Subj: Department of Defense Inspector General Draft Report
D-2007-D000FN-0216.000, "Internal Controls Over the
United States Marine Corps Military Equipment Baseline
Valuation Effort," dated August 27, 2008

Ref: (a) DODIG memo of August 27, 2008

Encl: (1) Marine Corps comments

1. In accordance with reference (a), the Marine Corps has reviewed the subject draft report and provides comments at the enclosure.
2. Point of contact for this matter is Mr. Charles Keith Dove, email charles.dove@usmc.mil or phone (703) 614-4500, DSN 224-2595.

A handwritten signature in black ink, appearing to read "C. K. Dove".

C. K. DOVE

By direction of the
Commandant of the Marine Corps

Department of Defense Inspector General Draft Report
D-2007-D000FN-0216.000, "Internal Controls Over the
United States Marine Corps Military Equipment Baseline
Valuation Effort," dated August 27, 2008

1. The Marine Corps has reviewed the draft report. Technical comments and responses to the audit recommendations are provided below.

The Marine Corps Systems Command (MARCORSYSCOM) disagrees with the major audit finding that the Marine Corps did not have adequate controls in place over the USMC military equipment baseline. The Marine Corps followed the OSD Property and Equipment Policy Office (P&EPO) guidance for establishing the initial valuation of all known military equipment (ME) programs. MARCORSYSCOM Program Managers (PMs) completed the questionnaires for the programs identified by P&EPO. To minimize the impact of the massive data collection effort on PMs, P&EPO provided on site contractor support to ensure the questionnaire responses were complete and collect the supporting documentation. KPMG LLP, was on site with the PMs for almost two years collecting documentation. KPMG spent six to eight weeks with each PM assimilating binders of supporting documentation for each program. Ultimately, P&EPO established the initial valuation of the equipment using this material. The documentation was turned over to KPMG by the Marine Corps and should have been retained by KPMG. It is impossible for the Marine Corps to recreate every document that was collected by KPMG during 2003 through 2005 as adequate support for the equipment valuation. If this information is no longer available from KPMG, the P&EPO approved questionnaires should serve as acceptable documentation for the inventory value as of September 30, 2006. The May 25, 2006 letter signed jointly by USD(C) and USD(AT&L) states that the Department reached a major milestone on December 31, 2005 by completing the initial valuation of all known military equipment (ME) programs. The documentation was determined to be adequate at that time.

From the point of the initial valuation effort, MARCORSYSCOM has complied with the P&EPO guidance for maintaining the equipment valuation information in the Capital Asset Management System - Military Equipment (CAMS-ME) beginning with FY 2007. Specifically, asset additions, disposals and transfers are recorded in CAMS-ME and supporting documentation is maintained by the MARCORSYSCOM point of contact for Military Equipment Valuation (MEV). MARCORSYSCOM has also provided both budget exhibit information and accounting system information to the P&EPO contractor on an ad hoc basis as requested to support the unit cost of the equipment; however, the Marine Corps does not have visibility over the way this information is used by P&EPO

Encl (1)

Department of Defense Inspector General Draft Report
D-2007-D000FN-0216.000, "Internal Controls Over the
United States Marine Corps Military Equipment Baseline
Valuation Effort," dated August 27, 2008

to determine the military equipment value. MARCORSYSCOM can attest to the accuracy of the documents, but only P&EPO can attest to how this information is used to calculate the equipment value. Therefore, as stated below, the Marine Corps nonconcur with Recommendation 1 that MARCORSYSCOM maintain the military equipment valuations; this must be a P&EPO responsibility because P&EPO is determining how to value the equipment from various data sources. The Marine Corps also nonconcur with Recommendation 2 that MARCORSYSCOM should review the initial waived programs. This was the determination made by P&EPO at the time the initial inventory value was determined.

Overall, the Marine Corps is concerned with the lack of official policies and accountability for the MEV process. P&EPO retains responsibility for most of the information in CAMS-ME and the Marine Corps has no visibility into how equipment valuations are determined based on that information. MARCORSYSCOM can be accountable for the source documentation it provides to populate CAMS-ME, but it cannot be accountable for the information produced after that point.

Recommendation 1. DODIG recommends that the Commander, Marine Corps Systems Command and Program Executive Officer Land Systems ensure that program managers maintain required documentation to support military equipment valuations, acquisition and disposal dates, useful lives, waivers, and program completeness.

Marine Corps Response: Nonconcur. This is a P&EPO responsibility.

Recommendation 2. DODIG recommends that the Commander, Marine Corps Systems Command and Program Executive Officer Land Systems ensure that program managers review waived programs as required and maintain documentation to support the military equipment waiver status.

Marine Corps Response: Nonconcur. This is a P&EPO responsibility.

Department of Defense Inspector General Draft Report
D-2007-D000FN-0216.000, "Internal Controls Over the
United States Marine Corps Military Equipment Baseline
Valuation Effort," dated August 27, 2008

Recommendation 3. DODIG recommends that the Commander, Marine Corps Systems Command and Program Executive Officer Land Systems ensure that program managers implement the management controls established by Property and Equipment Policy Office, Acquisition, Technology, and Logistics and United States Marine Corps Headquarters policy statements, directives, and regulations.

Marine Corps Response: Concur. The Commander, Marine Corps Systems Command has implemented controls to support all asset information provided to P&EPO. We consider this recommendation closed.

Clarified Page 10



Inspector General Department of Defense

