

Audit



Report

OFFICE OF THE INSPECTOR GENERAL

CONSOLIDATED FINANCIAL REPORT ON THE
NATIONAL GUARD AND RESERVE EQUIPMENT
APPROPRIATION FOR THE ARMY NATIONAL GUARD

Report No. 97-047

December 13, 1996

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Department of Defense

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Acronyms

| | |
|---------|--|
| ANGAS | Army National Guard Accounting System |
| ARNG | Army National Guard |
| DFAS-IN | Defense Finance and Accounting Service-Indianapolis Center |
| NGREA | National Guard and Reserve Equipment Appropriation |



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
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December 13, 1996

**MEMORANDUM FOR CHIEF, NATIONAL GUARD BUREAU
AUDITOR GENERAL, DEPARTMENT OF THE ARMY**

**SUBJECT: Audit Report on the Consolidated Financial Report on the National Guard
and Reserve Equipment Appropriation for the Army National Guard
(Report No. 97-047)**

We are providing this audit report for review and comment. We considered management comments on a draft of this report in preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. Management comments on a draft of this report were partially responsive. We request additional comments on the need to remove an account from the Army National Guard general ledger account structure and on planned actions regarding Recommendations 2.a., 2.c., and 2.d. We also request additional comments regarding procedures to ensure that liabilities are recorded for military equipment received in advance of payment. We request that the National Guard Bureau provide the additional comments by January 28, 1997.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Ms. Mary Lu Ugone, Audit Program Director, at (703) 604-9529 (DSN 664-9529) or Mr. John M. Donnelly, Audit Project Manager, at (703) 604-9549 (DSN 664-9549). See Appendix D for the report distribution. The audit team members are listed inside the back cover.

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Office of the Inspector General, DoD

Report No. 97-047
(Project No. 6RE-2016.03)

December 13, 1996

Audit of the Consolidated Financial Report on the National Guard and Reserve Equipment Appropriation for the Army National Guard

Executive Summary

Introduction. The audit was performed in compliance with the Chief Financial Officers' Act of 1990 (Public Law 101-576) and the Federal Financial Management Act of 1994 (Public Law 103-356). Public Law 103-356 requires DoD and other Government agencies to prepare consolidated financial statements for FY 1996 and each succeeding year. In a memorandum dated June 6, 1995, the DoD Deputy Chief Financial Officer informed DoD Components of the requirements to prepare and submit financial statements in accordance with the Federal Management Act of 1994.

In 1981, Congress established the National Guard and Reserve Equipment Appropriation (Department 97 funds*) to provide the equipment needed to maintain the readiness of the Army National Guard. Using that appropriation, the Under Secretary of Defense (Comptroller) allocated the Army National Guard \$120.8 million in FY 1995 and \$100 million in FY 1996. The Army National Guard reported assets, liabilities, and equity of \$750.1 million, \$5.1 million, and \$745.0 million respectively, as of September 30, 1995 for the Equipment Appropriation.

Audit Objectives. The primary audit objective was to evaluate the financial information the Army National Guard reported on its use of National Guard and Reserve Equipment Appropriation funds. We also evaluated the Army National Guard management control procedures for recording transactions in its standard general ledger accounts.

Audit Results. The Army National Guard did not properly record and report transactions in the general ledger. The Army National Guard duplicated reporting of military equipment, misstated liabilities, and incorrectly used a budgetary account. In addition, the Army National Guard did not record accounts payable upon evidence of equipment receipt.

As a result, the September 30, 1995, general ledger account balances for the Army National Guard contained the following misstatements:

o account 1722, Construction in Progress-Contractor, was overstated by \$427.1 million;

*The Department of the Treasury uses department code "97" to identify appropriations for the Office of the Secretary of Defense. The National Guard and Reserve Equipment Appropriation is considered a Department 97 appropriation.

o account 2111, Accounts Payable-Government-Current was overstated by \$5.4 million; account 2113, Accounts Payable-Public-Current was understated by \$321,000; and account 4910, Accrued Expenditures Unpaid-Direct Program was overstated by \$5.1 million; and

o account 4584, Anticipated Earned Authority-Defense Business Operations Fund, was incorrectly used to record allotted authority of \$323.3 million.

The Army National Guard could improve its management control program by accurately recording and reporting its National Guard and Reserve Equipment Appropriation funds and by maintaining subsidiary ledgers to support general ledger account balances (Appendix A). Implementation of the recommendations in the report will result in more accurate and meaningful reporting of financial data from the National Guard and Reserve Equipment Appropriation.

Summary of Recommendations. We recommend that the Army National Guard make adjusting entries to correct general ledger account balances and establish adequate controls to prevent duplicate recording and reporting of military equipment, to record liabilities for military equipment received in advance of payment, to record accounts payable only for transactions representing legitimate Army National Guard liabilities, and to reclassify allotments received.

Management Comments. The National Guard Bureau concurred with recommendations to make adjusting accounting entries to correct various proprietary and budgetary account balances, stating that the adjusting entries were made.

Although the National Guard Bureau partially concurred with the recommendation to develop and implement procedures to record and manage liabilities for military equipment purchased with National Guard and Reserve Equipment appropriated funds, the National Guard Bureau stated that the Army National Guard lacked the visibility over receipt of equipment needed to record the liabilities.

The National Guard Bureau partially concurred with recommendations to develop and implement procedures to prevent duplicate recording and reporting of military equipment, to verify that transactions recorded as liabilities are legitimate liabilities, and to periodically verify that crosswalk procedures from budget execution systems to general ledger account structures result in the complete and accurate transfer of financial information to general ledger accounts. However, the National Guard Bureau did not comment on actions taken or planned to implement the recommendations.

Audit Response. The National Guard Bureau comments were generally responsive except it did not comment on one recommendation to remove an account from the general ledger account structure and additional comments are needed to clarify actions on other recommendations. We ask that the National Guard Bureau provide additional comments on the recommendations to remove an account from the Army National Guard general ledger account structure, to implement procedures to ensure that liabilities are recorded for military equipment received in advance of payment, to develop procedures to prevent duplicate recording and reporting of military equipment, to verify the legitimacy of recorded liabilities, and to periodically verify crosswalk procedures from budget execution systems to general ledger account structures. We request that the National Guard Bureau provide additional comments by January 28, 1997.

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Part I - Audit Results

Audit Background

The audit was performed as part of the Chief Financial Officers' Act of 1990 (Public Law 101-576), which established requirements for Federal organizations to submit audited financial statements to the Director, Office of Management and Budget. Public Law 103-356, "The Federal Financial Management Act of 1994," requires DoD and other Government agencies to prepare consolidated financial statements for FY 1996 and each succeeding year. In the FY 1996 consolidated DoD financial statements, the Defense agencies and Military Departments will account for Department 97¹ funds as "Other Defense Organizations." The National Guard and Reserve Equipment Appropriation (NGREA) is included in "Other Defense Organizations."

In 1981, Congress established the NGREA to provide the equipment needed to maintain the readiness of the Army National Guard (ARNG). The Under Secretary of Defense (Comptroller) allocated the ARNG \$100 million in FY 1996 and \$120.8 million in FY 1995. The NGREA is a multi-year appropriation, normally available for obligation for 3 years.

NGREA Equipment Accounting

The ARNG records NGREA transactions in the State Accounting, Budgeting, Expenditure and Reservations System and maintains a general ledger account structure in the Army National Guard Accounting System (ANGAS). The ARNG developed a computer program that converts budget transactions from the State Accounting, Budgeting, Expenditure and Reservations System to ANGAS general ledger accounts on a monthly basis.

In addition to accounting for NGREA, the ARNG maintains an ANGAS general ledger account structure for property, plant, and military equipment assets. The ARNG updates the balances for those accounts quarterly. The state National Guard units report their total quarterly military equipment balances, based on state property book systems, through the ARNG Logistics Directorate to the ARNG Comptroller Directorate. The ARNG Comptroller Directorate manually enters the total equipment data into the ANGAS and reports that data to the Defense Finance and Accounting Service Indianapolis Center (DFAS-IN).

¹The Department of the Treasury uses department code "97" to identify appropriations for the Office of the Secretary of Defense. The National Guard and Reserve Equipment Appropriation is considered a Department 97 appropriation.

Financial Reporting

The ARNG provides the DFAS-IN monthly and fiscal yearend trial balances on NGREA funds. The ARNG also provides the DFAS-IN quarterly and fiscal yearend trial balances for property, plant, and equipment.

Audit Objectives

The primary audit objective was to evaluate the financial information the ARNG reported on its use of Department 97 funds from the NGREA. We also evaluated the Army National Guard management control procedures for recording transactions in its standard general ledger accounts. See Appendix A for the discussion of the audit scope, methodology, and the review of the management control program.

Appendix B discusses the need for improved guidance for general ledger account 1015, Undistributed Disbursements.

Army National Guard Accounting for NGREA

The ARNG did not correctly record and report NGREA transactions in the FY 1995 general ledger. The ARNG:

- o duplicated the recording and reporting of military equipment acquisitions and used an inappropriate real property asset account to record the acquisitions;

- o did not record accounts payable upon evidence of receipt of equipment and recorded accounts payable for transactions that did not establish Government liabilities; and

- o used an inappropriate budgetary allotment account for anticipating reimbursable authority earned during the year.

These conditions occurred because ARNG did not establish adequate controls to prevent or detect duplicate recording and reporting of military equipment assets and to ensure that liabilities were recorded for military equipment received in advance of payment. In addition, ARNG used an inaccurate crosswalk² from the budget execution system and did not establish subsidiary accounting ledgers to support account balances.

As a result, the ARNG general ledger accounts for the period ended September 30, 1995, included the following misstatements.

- o Account 1722, Construction in Progress-Contractor, was overstated by \$427.1 million.

- o Account 2111, Accounts Payable-Government-Current, was overstated by \$5.4 million; account 2113, Accounts Payable-Public-Current, was understated by \$321,000; and account 4910, Accrued Expenditures-Unpaid-Direct Program, was overstated by \$5.1 million.

- o Account 4584, Anticipated Earned Authority-Defense Business Operations Fund, was incorrectly used to record allotted authority of \$323.3 million.

²The ARNG developed a computer program that retrieves data from the State Accounting, Budgeting, Expenditures, and Reservations System and classifies the data into predetermined general ledger accounts. The term "crosswalk" is commonly used in the financial community to describe that process.

General Ledger Financial Recording Requirements

DoD 7000.14-R, "Financial Management Regulation" (the Regulation), volume 1, "General Financial Management Information, Systems, and Requirements," May 1993, and volume 4, "Accounting Policy and Procedures," January 1995, establish responsibilities, requirements, principles, standards, systems, procedures, and practices necessary to comply with financial management statutory and regulatory requirements applicable to the DoD. The Regulation covers all appropriated, nonappropriated, working capital, revolving, and trust fund activities.

Also, the Regulation, volume 1, states that each accounting system shall include adequate controls to promote the accuracy of accounts. The Regulation requires organizations to implement controls needed to ensure that data needed in an accounting system shall be entered only once and be transferred to appropriate accounts.

DFAS-IN Regulation 37-1, "Finance and Accounting Policy Implementation," September 18, 1995, implemented the Financial Management Regulation for Army organizations and established accounting, fund control, disbursing, and travel policy and procedures for all levels of Army resource management.

Military Equipment. The Regulation, volume 4, states that equipment consists of all personal property owned by DoD that is not a part of real property and that asset account 1760, Military Equipment, should be used to record the capitalized³ value of DoD military equipment that has been issued for use. The Regulation states that account 1722, Construction in Progress-Contractor, should be used to accumulate costs of DoD real property construction accounts, such as buildings and structures. Military equipment items should not be included in that account, unless the equipment is an integral part of the real property and could not be removed without dismantling the property.

Accounts Payable. The Regulation, volume 4, states that recording of accounts payable is generally the first transaction level entry in proprietary general ledger accounts. The Regulation also states that accounting organizations should record accounts payable upon evidence of receipt of equipment purchased. The Regulation further states that the recording of accounts payable shall be based on receiving reports, inspection reports, or other satisfactory evidence of performance that clearly shows quantities received and accepted by DoD.

Allotment Authority. DFAS-IN Regulation 37-1 defines allotments as the amount authorized by the agency head to the head of a lower level to incur obligations. General ledger account 4580.1, Allotted Direct Authority-Current Period-Basic, should carry a positive balance to represent the amount of direct and specifically apportioned allotments received for the fiscal year.

³Property purchased is "capitalized" when it is recorded as an asset in financial accounting records. The cost of property not capitalized is recorded as a current operating expense. (Current capitalization threshold is \$100,000.)

Army National Guard General Ledger

The Army National Guard duplicated general ledger recordings of military equipment, did not record liabilities for military equipment received and accepted in advance of payment, incorrectly recorded liabilities for transactions that did not establish indebtedness, and used inappropriate proprietary and budgetary accounts to record transactions. The table below lists the nine general ledger accounts the ARNG reported to the DFAS-IN for FY 1995.

NGREA General Ledger Account Balances

| <u>Account Number</u> | <u>Account</u> | <u>Amount</u> |
|---------------------------|---|---------------|
| 1013 | Fund Balance with Treasury | \$323,346,153 |
| 1722 | Construction in Progress-Contractor | 427,096,653 |
| 2111 | Accounts Payable-Government-Current | (5,459,662) |
| 2113 | Accounts Payable-Public-Current | 321,144 |
| 3100 | Appropriated Capital | (745,304,289) |
| 4584 | Anticipated Earned Authority-Defense Business Operations Fund | 323,346,152 |
| 4611 | Uncommitted/Unobligated Allotments-Direct Program-Current Period | 22,808,218 |
| 4811 | Undelivered Orders-Direct Program | (341,015,852) |
| 4910 | Accrued Expenditures-Unpaid-Direct Program | (5,138,517) |

Duplicate Recording of Military Equipment Assets. The ARNG recorded and reported to the DFAS-IN \$427.1 million for NGREA military equipment acquisitions in ANGAS general ledger account 1722, Construction in Progress-Contractor. The ARNG reported that amount even though the ARNG maintained another official general ledger account structure, also transmitted to DFAS-IN, which included the cost of all ARNG-owned military equipment acquisitions. Consequently, the ARNG provided the DFAS-IN duplicate financial information on use of NGREA funds.

Military Equipment General Ledger Account Structure. The ARNG provided a quarterly general ledger report to the DFAS-IN on general ledger account balances for military equipment owned by each ARNG reporting unit. ARNG accounting officials obtained the quarterly military equipment balances from the ARNG Logistics Directorate and updated military equipment general ledger account balances maintained in the ANGAS before transmitting the general ledger information to the DFAS-IN. The ARNG September 30, 1995, report (adjusted) to the DFAS-IN showed a military equipment balance of \$34.2 billion. That balance included the \$427.1 million reported in general ledger account 1722, Construction in Progress-Contractor.

General Ledger Account for Equipment. The ARNG used an inappropriate general ledger account, account 1722, Construction in Progress-Contractor, to record purchases of military equipment from disbursements of NGREA funds. Military equipment transactions should not be included in that account, unless the equipment is an integral part of real property and the equipment normally could not be removed without dismantling the property. The ARNG did not use NGREA funds to acquire equipment attached to real property.

Controls over Equipment Accounts. The ARNG had not established control mechanisms to ensure that general ledger military equipment account balances recorded and reported to the DFAS-IN were not also included in the general ledger account structure for the NGREA. Further, the ARNG did not have controls to ensure that military equipment data were entered into the ANGAS only once. As a result, the ARNG inappropriately used account 1722, Construction in Progress-Contractor, to record military equipment acquisitions.

Recording of Liabilities. The ARNG did not record liabilities for military equipment received in advance of payment. ARNG accounting officials did not receive evidence of receipt and acceptance of military equipment and, therefore, were unable to record liabilities for equipment acquired, but not yet paid for. The Regulation, volume 4, requires that accounts payable transactions be based on satisfactory evidence of performance that clearly shows quantities received and accepted by DoD.

We did not attempt to determine the extent to which NGREA acquisitions were delivered and accepted before payment because the ARNG did not have adequate systems in place to perform efficient audit tests (see Appendix A). However, ARNG accounting and logistics officials told us that military equipment is usually received in advance of payment.

Recording Payments as Liabilities. The ARNG inappropriately recorded and reported \$5.1 million of liabilities for NGREA transactions that were, in fact, payments to contractors. The ARNG incorrectly recorded liabilities totaling \$5.1 million in general ledger account 2111, Accounts Payable-Government-Current and general ledger account 2113, Accounts Payable-Public-Current. In addition, the ARNG recorded \$5.1 million of budgetary accruals in the corresponding budgetary account, account 4910, Accrued Expenditures-Unpaid-Direct Program.

The ARNG had not established procedures to ensure that liabilities were recorded only for budget transactions that established ARNG indebtedness. ARNG officials stated that they were aware of the incorrect recording and reporting of liabilities, but did not make adjustments to budget data because of other priorities. As a result, account 2111, Accounts Payable-Government-Current, was overstated by \$5.4 million; account 2113, Accounts Payable-Public-Current, was understated by \$321,000; and account 4910, Accrued Expenditures-Unpaid-Direct Program, was overstated by \$5.1 million.

Classifying Allotments. The ARNG recorded and reported \$323.3 million of allotted direct program authority in general ledger account 4584, Anticipated

Earned Authority-Defense Business Operations Fund, even though the NGREA was not a Defense Business Operations Fund. The ARNG should have used general ledger account 4580.1, Allotted Direct Authority-Current Period-Basic, to record the NGREA allotments.

The ARNG had not updated the ANGAS crosswalk to comply with current DoD accounting classifications. The ARNG crosswalk process followed an outdated regulation to classify basic allotments received into account 4584, Anticipated Earned Authority-Defense Business Operations Fund. However, DFAS-IN Regulation 37-1 requires accounting organizations to use account 4580.1, Allotted Direct Authority-Current Period-Basic, to record basic allotments received. DFAS-IN Regulation 37-1 requires organizations to use account 4584 as a summary account for organizations operating on a revolving fund basis. Account 4584 should not be used to account for NGREA acquisitions of equipment. Therefore, the ARNG should transfer the balance in budgetary account 4584, Anticipated Earned Authority-Defense Business Operations Fund, to account 4580.1, Allotted Direct Authority-Current Period-Basic. In addition, the ARNG should remove account 4584 from the NGREA account structure in the ANGAS.

Maintaining Subsidiary Accounting Ledgers. The ARNG did not maintain required transaction-based subsidiary ledgers to support general ledger account balances. The Regulation, volume 1, chapter 3, May 1993, requires accounting systems to have general ledger control and a DoD-approved account structure and to list subsidiary general ledger accounts that must be reconciled to a control account at least monthly. We did not make recommendations to correct this weakness because the ARNG was implementing corrective actions. See Appendix A for further discussion of this weakness, its effect on the audit scope, and the corrective action.

Recommendations, Management Comments, and Audit Response

We recommend that the Director, Army National Guard:

- 1. Make adjusting accounting entries to:**
 - a. Eliminate the balance in account 1722, Construction in Progress-Contractor, and remove that account from the National Guard and Reserve Equipment Appropriation general ledger account structure.**
 - b. Eliminate all current FY 1996 balances in account 2111, Accounts Payable-Government-Current; account 2113, Accounts Payable-Public-Current; and account 4910, Accrued Expenditures-Unpaid-Direct Program, which do not represent liabilities for military equipment.**

c. Transfer the current FY 1996 balance in account 4584, Anticipated Earned Authority-Defense Business Operations Funds, to account 4580.1, Allotted Direct Authority-Current Period-Basic, and remove account 4584 from the National Guard and Reserve Equipment Appropriation general ledger account structure.

Management Comments. The National Guard Bureau (the Guard) concurred with Recommendations 1.a., 1.b., and 1.c., stating that account balances were either eliminated or transferred to appropriate general ledger accounts.

Audit Response. The Guard comments on Recommendations 1.a. and 1.b. were fully responsive, and the comments on Recommendation 1.c. were partially responsive. The Guard did not comment on the need to remove account 4584 from the ARNG general ledger account structure. Therefore, we request that the Guard provide additional comments on Recommendation 1.c. in response to the final report.

2. Develop and implement accounting procedures to:

a. Prevent duplicate recording and reporting of military equipment.

b. Obtain adequate evidence of receipt and acceptance of military equipment purchased with National Guard and Reserve Equipment Appropriation funds to record and manage liabilities.

c. Verify that transactions recorded in liability accounts represent legitimate Army National Guard liabilities.

d. Periodically verify that crosswalk procedures from budget execution systems to general ledger account structures result in the complete and accurate transfer of financial information to general ledger accounts and comply with current DoD accounting policy and procedures.

Management Comments. The Guard partially concurred with Recommendations 2.a., 2.c., and 2.d., but did not provide the corrective actions taken or planned.

The Guard partially concurred with Recommendation 2.b. The Guard stated that even though ARNG field organizations receive military equipment several months prior to receipt of disbursement transactions, the ARNG does not record liabilities for the equipment because the ARNG lacks visibility over the receipt of military equipment. The ARNG usually receives payment notices several months after ARNG organizations receive equipment. For military equipment acquisitions costing more than \$1 million, the ARNG establishes liabilities in advance of payment because ARNG accounting officials must validate the availability of funds before disbursement by the payment office.

Audit Response. The Guard comments are partially responsive on Recommendations 2.a., 2.c., and 2.d. We request that the Guard provide the actions planned or taken to develop and implement procedures to prevent

Army National Guard Accounting for NGREA

duplicate recording and reporting of military equipment, to verify the legitimacy of recorded liabilities, and to periodically verify crosswalk procedures from budget execution systems to general ledger account structures in response to the final report.

Although the Guard partially concurred with Recommendation 2.b., the comments are not responsive. Regarding the ARNG lack of visibility over the receipt of military equipment, the ARNG needs to implement procedures to ensure that financial records disclose liabilities for military equipment received, but not paid for because the Regulation, volume 4, "Accounting Policy and Procedures," January 1995, requires DoD Components to record liabilities for military equipment upon evidence of receipt. Therefore, we request that the Guard provide additional comments on Recommendation 2.b. in response to the final report.

Part II - Additional Information

Appendix A. Audit Process

Scope

We reviewed the ARNG process for recording and reporting FY 1995 financial transactions executed with funds from the National Guard and Reserve Equipment Appropriation (NGREA) for FYs 1988 through 1995. The ARNG received NGREA funds totaling about \$2.7 billion during that period. Also, we evaluated ARNG financial operations and internal controls. The ARNG reported NGREA assets, liabilities, and equity totaling \$750.1 million, \$5.1 million, and \$745.0 million, respectively, as of September 30, 1995. The audit was performed as part of the Chief Financial Officers Act of 1990 (Public Law 101-576), which established requirements for Federal organizations to submit audited financial statements to the Director, Office of Management and Budget.

We interviewed personnel at the ARNG and the DFAS-IN. We also spoke with personnel at the Office of the Under Secretary of Defense (Comptroller); Office of the Assistant Secretary of the Army (Financial Management and Comptroller); Military District of Washington, District of Columbia; and Defense Financial Accounting Service, Arlington, Virginia.

Scope Limitation. We limited the extent of testing the accuracy of general ledger account balances because ARNG accounting systems did not have transaction-based subsidiary ledgers to support account balances. The lack of subsidiary ledgers is a material departure from key accounting requirement number 1, General Ledger Control, and key accounting requirement number 8, Audit Trails. Those two requirements are identified in DoD 7000.14-R, "Financial Management Regulation," volume 1, "General Financial Management Information, Systems, and Requirements," May 1993. Even though we limited the extent of our testing, we performed analytical tests and other auditing procedures to determine the appropriateness of general ledger accounts and related balances the ARNG used.

Computer-Processed Data. We relied on computer-processed data from the ARNG September 30, 1995, general ledger report and from September 30, 1995, budgetary reports to evaluate the ARNG general ledger account structure. Due to the scope limitations discussed above, we were unable to use the computer-processed data to verify the accuracy of account balances.

Audit Period and Standards. We performed this financial-related audit from March through September 1996 in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD, and accordingly included such tests of management controls as were considered necessary.

Methodology

To evaluate the ARNG process for recording and reporting FY 1995 financial information on NGREA funds, we:

- o reviewed DoD, DFAS-IN, and ARNG policies and procedures;
- o interviewed responsible ARNG officials to determine procedures used to obtain, record, report, and reconcile NGREA funds;
- o analyzed September 30, 1995, budgetary reports;
- o analyzed the ARNG September 30, 1995, general ledger report;
- o analyzed the ANGAS crosswalk from budgetary reports to the general ledger; and
- o compared the ARNG process for recording the NGREA transactions in general ledger budgetary and proprietary accounts with techniques prescribed by DoD regulations.

Prior Audit Coverage

Office of the Inspector General, DoD, Report No. 97-044, "Army National Guard Military Equipment," December 11, 1996. The report states that the ARNG recorded military equipment items in general ledger accounts that were below the Army capitalization threshold and, therefore, overstated the military equipment account by \$9.1 billion, and misclassified \$1.2 billion of equipment in transit as equipment in use. The report also identifies material management control weaknesses related to reporting of military equipment. The report recommends that the ARNG record and report the value of military equipment using established capitalization thresholds and classification criteria, and document procedures for recording and reporting military equipment transactions. The report also recommends that the DFAS-IN make appropriate accounting entries to accurately classify ARNG military equipment in the Army general ledger. The Army National Guard concurred with the recommendations and proposed corrective actions that are fully responsive, and will take additional actions to strengthen its management control program. The DFAS-IN nonconcurred with the recommendation to make appropriate accounting entries; however, DFAS-IN proposed corrective actions that are responsive to the intent of the recommendation.

Management Control Program

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, requires DoD organizations to implement a comprehensive strategy for management controls that provides reasonable assurance that revenues and expenditures applicable to DoD operations are properly recorded and accounted for to permit preparation of accounts and reliable financial reports. DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996, requires each DoD Component to develop a management control program that: establishes the management control process; segments the organization into assessable units; and evaluates, identifies, and reports on management control weaknesses. The Directive also states that specific DoD policies for evaluating accounting system controls are in DoD 7000.14-R, "Financial Management Regulation," volume 1, chapter 3, May 1993. The Regulation requires accounting system managers to perform annual reviews of accounting system controls to determine compliance with key accounting requirements specified in the Regulation.

Scope of Review of Management Control Program. We reviewed the ARNG Comptroller Directorate's FY 1995 annual review of accounting system controls to determine whether the ARNG:

- o evaluated financial system compliance with key accounting requirements;
- o identified material departures from key accounting requirements; and
- o recorded a plan of corrective action for identified material departures.

Adequacy of Management Controls. We identified material management control weaknesses, as defined by DoD Directive 5010.38, for the ARNG. The ARNG did not properly record and report transactions in the general ledger and did not maintain subsidiary ledgers to support general ledger account balances. Recommendation 2. in the report, if implemented, and a pending ARNG accounting system modification to include automated subsidiary ledgers, will correct the material weaknesses. A copy of this report will be provided to the senior official responsible for management controls in the ARNG.

Adequacy of Management's Self-Evaluation. The ARNG identified fiscal accounting as an assessable unit and, in our opinion, correctly identified the risk associated with key accounting requirement 1, General Ledger Control and Financial Reporting, as high. ARNG officials identified and reported in the FY 1995 Annual Statement of Assurance the material weakness identified by the audit and is working with the DFAS-IN to deploy the Corps of Engineers Financial Management System to correct the weakness. ARNG officials did not provide a date for full implementation of that accounting system.

Appendix B. Reporting Requirements for Undistributed Disbursements

The guidance in the Financial Management Regulation and in the DFAS-IN Regulation 37-1 was incomplete or unclear as to reporting requirements for account 1015, Undistributed Disbursements. As a result, the ARNG FY 1995 Department of the Army general ledger, maintained by the DFAS-IN, may include incorrect balances for account 1015.

The Financial Management Regulation, volume 1, May 1993, defines undistributed disbursements as the amount of disbursements reported by the finance network not yet accepted by the operating level accounting entity. The DFAS-Columbus Center, the payment office for the ARNG, reported FY 1995 account 1015 debit balances of \$250 million to the DFAS-IN. However, the ARNG, the operating level accounting entity, recorded \$362 million in credits in its general ledger, but did not report those credits to the DFAS-IN. Therefore, the ARNG general ledger maintained by the DFAS-IN may have included an abnormal debit balance in account 1015.

This condition occurred because DFAS-IN Regulation 37-1, "Finance and Accounting Policy Implementation," September 18, 1995, did not have clear reporting requirements. Regulation 37-1 requires financing and accounting offices to close account 1015 as part of the yearend closing process, but does not specify whether account 1015 balances should be closed before or after transmission of trial balances to the DFAS-IN. The ARNG closed the FY 1995 balance in account 1015 before transmission of the ARNG FY 1995 trial balance to the DFAS-IN, and the DFAS-Columbus Center transmitted account 1015 balances to the DFAS-IN.

The Financial Management Regulation, volume 4, chapter 2, "Accounting For Cash and Fund Balance With Treasury" included account 1015 under section 0205, Disbursement Policy, but the Regulation does not discuss accounting entries for account 1015. The Regulation states that account 1015 guidance would be published, but does not specify the expected date of publication. We will provide additional audit coverage of account 1015 upon publication of DoD guidance on the account.

Appendix C. Report Distribution

Office of the Secretary of Defense

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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

National Guard Bureau Comments



DEPARTMENTS OF THE ARMY AND THE AIR FORCE
NATIONAL GUARD BUREAU
111 SOUTH GEORGE MASON DRIVE
ARLINGTON, VA 22204-1382

NGB-ARC

19 Nov 96

MEMORANDUM THRU

25 NOV 1996
0158-FO 11/27/96
DIRECTOR, ARMY STAFF (DAS) THE PENTAGON, WASHINGTON, DC 20310
ASSISTANT SECRETARY OF THE ARMY FOR FINANCIAL MANAGEMENT AND
CONTROLLER (ASA-FM&C), THE PENTAGON, WASHINGTON, DC 20310

FOR DEPARTMENT OF DEFENSE INSPECTOR GENERAL (DODIG), DIRECTOR,
READINESS AND OPERATIONAL SUPPORT DIRECTORATE, 400
ARMY NAVY DRIVE, ARLINGTON, VA 22202-2884

SUBJECT: Audit Report on Consolidated Financial Report on the
National Guard and Reserve Equipment Appropriation for the Army
National Guard (Project No. 6RE-2016.03)

1. The following management comments are provided relative to
subject audit:

Finding: The Army National Guard (ARNG) did not correctly
record and report National Guard and Reserve Equipment
Appropriation (NGREA) transactions in the FY 1995 general
ledger.

Recommendation-1. "Make adjusting accounting entries to:

a. Eliminate the balance in account 1722, Construction in
Progress-Contractor, and remove that account from the National
Guard and Reserve Equipment Appropriation general ledger account
structure.

b. Eliminate all current FY 1996 balances in account 2111,
Accounts Payable-Government-Current; account 2113, Accounts
Payable-Public-Current; and account 4910, Accrued Expenditures-
Unpaid-Direct Program which do not represent liabilities for
military equipment.

c. Transfer the current FY 1996 balance in account 4584,
Anticipated Earned Authority-Defense Business Operations Funds,
to account 4580.1, Allotted Direct Authority-Current Period-
Basic, and remove account 4584 for the National Guard and
Reserve Equipment Appropriation general ledger account
structure."

NGB-ARC

SUBJECT: Audit Report on Army National Guard Military Equipment
(Project No. 6RE-2016.03)

Recommendation-2. "Develop and implement procedures to:

- a. Prevent duplicate recording and reporting of military equipment.
- b. Obtain adequate evidence of receipt and acceptance of military equipment purchased with National Guard and Reserve Equipment Appropriation funds to record and manage liabilities.
- c. Verify that transactions recorded in liability accounts represent legitimate Army National Guard liabilities.
- d. Periodically verify that crosswalk procedures from budget execution systems to general ledger account structures result in the complete and accurate transfer of financial information to general ledger accounts and comply with current DoD accounting policy and procedures."

Management Comments: Concur with findings and recommendations 1.a.through 1.c. Partially concur with recommendations 2.a.through 2.d. For FY 1996 general ledger reporting, we have eliminated all balances in accounts 1722, 2111, 2113, and 4910. The balance in account 4584 has been transferred to account 4580.1.

The verification of receipt and acceptance of military equipment purchased with NGREA funds, and the establishment of transactions in liability accounts present many difficulties of an operational nature. National Guard Reserve Equipment Account funds are executed through the use of Military Interdepartmental Purchase Requests (MIPRs) on a centralized basis. There is no direct contracting by the ARNG with commercial contractors for the purchase of military equipment supported by NGREA funds. Military Interdepartmental Purchase Requests are issued by the ARNG to other Army and DOD agencies (performing activities) for the purchase of military equipment. The performing activity will generally apply the ARNG NGREA funds received on the MIPR to existing contracts, or in some cases will re-issue a second MIPR to another Army or DOD agency. The equipment purchased is shipped directly to an ARNG unit located in one of the 54 States or territories where a property book entry is made creating a general ledger transaction in an asset account. The ARNG has no visibility over the liability (accounts payable) until a

National Guard Bureau Comments

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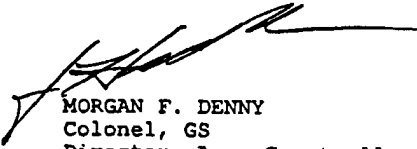
SUBJECT: Audit Report on Army National Guard Military Equipment
(Project No. 6RE-2016.03)

disbursement transaction is received directly from the performing activity, or the performing activity's servicing disbursing office. This could be several months after receipt of the equipment by an ARNG activity. When a disbursement transaction is received, an accounts payable will be established and simultaneously liquidated with the posting of the disbursement transaction. The exceptions are disbursements in excess of \$1M which must be prevalidated by the accounting station (ARNG). In these cases, a liability can be established in advance of the payment. Therefore, the only NGBEA related accounts payable will be for those prevalidated disbursements that have been approved for payment but not yet posted to the accounting records of the ARNG.

2. In regard to management controls, the ARNG accounting system has been identified as a material weakness in each NGB annual assurance statement of internal management controls since 1988. Specific ARNG accounting system deficiencies in general ledger accounting and reporting were identified in the FY 1996 annual review of accounting system controls, Key Accounting Requirement 1, submitted to Defense Finance Accounting Service-Indiana (DFAS-IN) in June 1996. To correct the deficiencies in the ARNG accounting system, we are working with DFAS-IN to deploy the Corps of Engineers Financial Management System (CEFMS) throughout the ARNG as a replacement for the current ARNG accounting system.

3. I appreciate the assistance provided by the DODIG audit staff during the April through September 1996 period of audit work. We will keep you posted on events that may affect areas covered by this audit. My points of contact are Ms. Pat Condon, or Mr. John Argodale, (703) 607-7704 or (703) 607-7510 respectively.

FOR THE CHIEF, NATIONAL GUARD BUREAU:



MORGAN F. DENNY
Colonel, GS
Director, Army Comptroller

CF:
ASA (FM&C)
DFAS-IN-AA
NGB-IR

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