

December 22, 2005



# Financial Management

Internal Controls Over the  
Compilation of the Air Force, General  
Fund, Fund Balance With Treasury  
for FY 2004  
(D-2006-039)

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### **Acronyms**

ASA	Annual Statement of Assurance
DDRS	Defense Departmental Reporting System
DDRS-AFS	DDRS-Audited Financial Statements
DDRS-B	DDRS-Budgetary
DFAS	Defense Finance and Accounting Service
FASAB	Federal Accounting Standards Advisory Board
FBWT	Fund Balance With Treasury
FMFIA	Federal Managers' Financial Integrity Act
FMR	Financial Management Regulation
GAFS-R	General Accounting and Finance System-Rehost
OMB	Office of Management and Budget
OUSDC(C)/CFO	Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer
SFFAS	Statement of Federal Financial Accounting Standards
SOP	Standard Operating Procedure
TFM	Treasury Financial Manual



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

December 22, 2005

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE  
(COMPTROLLER)/CHIEF FINANCIAL OFFICER  
ASSISTANT SECRETARY OF THE AIR FORCE  
(FINANCIAL MANAGEMENT AND COMPTROLLER)  
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING  
SERVICE DENVER

SUBJECT: Report on Internal Controls Over the Compilation of the Air Force, General Fund, Fund Balance With Treasury for FY 2004 (Report No. D-2006-039)

We are providing this report for review and comment. We considered management comments from the Deputy Chief Financial Officer and the Director of Defense Finance and Accounting Service on a draft of this report when preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The Deputy Chief Financial Officer comments were partially responsive on Recommendations A.1.a.(1)-(5), A.1.b.-f., D.1.a., and D.1.b.(1)-(2) and not responsive on Recommendations B.1.c.-e. and D.1.c.(1)-(2). Therefore, we request additional comments on these recommendations by January 23, 2006. The Director of Defense Finance and Accounting Service comments were not responsive on Recommendations B.2.b.(1)-(6) and E.1.a.-c. Therefore, we request additional comments on these recommendations by January 23, 2006.

If possible, please send management comments in electronic format (Adobe Acrobat file only) to [Auddfs@dodig.mil](mailto:Auddfs@dodig.mil). Copies of the management comments must contain the actual signature of the authorizing official. We cannot accept the / Signed / symbol in place of the actual signature. If you arrange to send classified comments electronically, they must be sent over the SECRET Internet Protocol Router Network (SIPRNET).

We appreciate the courtesies extended to the staff. Questions should be directed to Mr. Douglas Neville at (703) 428-1061 (DSN 664-1061) or Mr. Mark Henricks at (703) 428-1270 (DSN 664-1270). See Appendix K for the report distribution. The team members are listed inside the back cover.

By direction of the Deputy Inspector General for Auditing:

A handwritten signature in black ink, reading "Paul J. Granetto", is written over a horizontal line.

Paul J. Granetto, CPA  
Assistant Inspector General  
Defense Financial Auditing  
Service

## Department of Defense Office of Inspector General

Report No. D-2006-039

December 22, 2005

(Project No. D2005-D000FP-0074.000)

### Internal Controls Over the Compilation of the Air Force, General Fund, Fund Balance With Treasury for FY 2004

#### Executive Summary

**Who Should Read This Report and Why?** Defense Finance and Accounting Service (DFAS) personnel involved with the Fund Balance With Treasury (FBWT) account should read this report. This report contains guidance that DFAS can use to assess and validate the reporting of DoD and its Components' FBWT accounts on their financial statements.

**Background.** We performed this audit in support of Public Law 101-576, the "Chief Financial Officers Act of 1990," November 15, 1990, as amended by Public Law 103-356, the "Federal Financial Management Act of 1994," October 13, 1994, and Public Law 104-208, the "Federal Financial Management Improvement Act of 1996," September 30, 1996.

The Air Force General Fund (General Fund), Consolidated Balance Sheet reported \$60.6 billion in their FBWT account and \$243.1 billion in total assets as of September 30, 2004. The General Fund FBWT account represented 20.9 percent of the FBWT account reported on the DoD Agency-Wide Consolidated Balance Sheet as of September 30, 2004.

**Results.** Overall, DFAS Denver did not have adequate controls over the compilation process for the General Fund FBWT account as of September 30, 2004. We identified the following internal control weaknesses.

- DFAS Denver did not adequately reconcile General Fund expenditure and receipt accounts to expenditure and receipt accounts established and reported in Treasury reports. Specifically, DFAS Denver did not reconcile 113 (34 percent) of the 329 expenditure and receipt accounts established and reported by Treasury as of September 30, 2004. Of the 113 expenditure and receipt accounts not reconciled, 59 accounts were active at least once, 54 accounts never had activity,\* and 12 of the 59 accounts had activity during FY 2004 of \$10.9 billion (absolute). As a result, these unresolved differences compromised the reliability of the accounting records for DFAS Denver expenditure and receipt accounts. In addition, the lack of reconciliation further hinders preparation of General Fund auditable financial statements (finding A).

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\*19 of the 54 accounts were FY 2005 accounts, which were established by Treasury prior to the end of FY 2004.

- DFAS Denver did not have adequate internal controls for classifying expenditure accounts as entity or non-entity and by fund type. Specifically, DFAS Denver had to create multiple journal voucher adjustments after fiscal year-end in Defense Departmental Reporting System-Audited Financial Statements (DDRS-AFS) to classify expenditure accounts as entity or non-entity and by fund type. In particular, DFAS Denver made three journal voucher adjustments to assign the entity attribute and five journal voucher adjustments to assign the fund type attribute. Although the net effect of these journal voucher adjustments to the General Fund, FBWT account was \$79.3 million, a potential misclassification error of \$1.3 billion (absolute) may occur on the classification of expenditure accounts as entity or non-entity and by fund type. As a result, potential misstatements may occur on the financial statements. In addition, auditors were not able to perform a timely review of the General Fund financial statement compilation process; therefore, future audits of the General Fund financial statements may not be completed in the required 45-day timeframe (finding B).
- DFAS Denver did not adequately support any of the 14 journal voucher adjustments created in DDRS-AFS to adjust the September 30, 2004, General Fund FBWT account by \$1.5 billion (absolute). As a result, potential misstatements may occur on the financial statements (finding C).
- DFAS Denver incorrectly included \$6.9 million of Air Force transfers to the Department of Transportation, excluded \$16.1 million of transfers to the Air Force from the Office of Management and Budget and the Department of Agriculture, and included \$152 million in unavailable receipt accounts in Line 2.A., "Fund Balance per Treasury." As a result, DFAS Denver overstated the amount for Line 2.A., "Fund Balance per Treasury," in Note 3, "Fund Balance With Treasury," by \$142.8 million on the September 30, 2004, General Fund financial statements. Furthermore, DFAS Denver is not reporting the correct reconciling amount in Note 3, "Fund Balance With Treasury" (finding D).
- The DFAS Denver Management Control Program for FBWT was ineffective and did not identify and report material weaknesses for FBWT in their FY 2004 Annual Statement of Assurance. As a result, DFAS Denver cannot provide reasonable assurance that internal controls for the General Fund FBWT account are in place and operating effectively (finding E).

**Management Comments and Audit Response.** The Deputy Chief Financial Officer concurred with 22 of the recommendations and nonconcurred with 1 of the recommendations. The Director of DFAS concurred with 14 of the recommendations and nonconcurred with 9 of the recommendations. The Director of DFAS stated that none of the audit findings were proven to identify any material or substantive deficiencies. However, the Director of DFAS did not, for the most part, take exception to the improvements recommended in the audit report. The Deputy Chief Financial Officer comments were partially responsive to 13 recommendations and not responsive to 5 recommendations. The Director of DFAS comments were not responsive to nine recommendations. Therefore, we request that the Deputy Chief Financial Officer and the Director of DFAS provide comments on the final report by January 23, 2006. See the Finding sections of the report for a discussion of management comments and the Management Comments section of the report for the complete text of the comments.

# Table of Contents

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<b>Executive Summary</b>	i
<b>Background</b>	1
<b>Objectives</b>	3
<b>Management Control Program Review</b>	3
<b>Findings</b>	
A. Reconciliation of the Air Force General Fund Expenditure and Receipt Accounts	5
B. Expenditure Account Attributes	12
C. DDRS-AFS Journal Voucher Adjustments	21
D. Air Force, General Fund, Note 3, “Fund Balance With Treasury”	25
E. DFAS Denver Management Control Program for FBWT	33
<b>Appendixes</b>	
A. Scope and Methodology	38
B. Prior Coverage	41
C. Fund Balance With Treasury	42
D. Glossary	43
E. Treasury Fund Symbols and Expenditure and Receipt Accounts	45
F. Treasury Reports for Fund Balance With Treasury	49
G. List of Expenditure and Receipt Accounts Not Reconciled from the GAFS-R Trial Balance	51
H. Checklists for Reviewing Financial Management Systems	54
I. Hierarchy of Accounting Standards	56
J. Elements of a Management Control Program	57
K. Report Distribution	58
<b>Management Comments</b>	
Office of the Under Secretary of Defense	61
Defense Finance and Accounting Service	65

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## Background

We performed this audit in support of Public Law 101-576, the “Chief Financial Officers Act of 1990,” November 15, 1990, as amended by Public Law 103-356, the “Federal Financial Management Act of 1994,” October 13, 1994, and Public Law 104-208, the “Federal Financial Management Improvement Act of 1996,” September 30, 1996. See Appendix A for scope and methodology and Appendix B for prior coverage related to the objectives.

**Fund Balance With Treasury.** Fund Balance With Treasury (FBWT) is an asset account that represents a material line item on the September 30, 2004, General Fund and the DoD Agency-Wide Consolidated Balance Sheets. The General Fund FBWT account and total assets are material to the DoD Agency-Wide Consolidated Balance Sheet. Table 1 shows the percentages.

<b>Table 1. September 30, 2004 Consolidated Balance Sheet Extracts</b>			
	<u>General Fund</u>	<u>DoD Agency-Wide</u>	<u>Percentage of DoD Agency-Wide</u>
FBWT	\$ 60.6 billion	\$ 289.6 billion	20.9%
Total Assets	243.1 billion	1,208.5 billion	20.1%
FBWT as a Percentage of Total Assets	24.9%	24.0%	

Statement of Federal Financial Accounting Standards No. 1, “Accounting for Selected Assets and Liabilities,” March 30, 1993, defines an entity’s Fund Balance With Treasury as “... the aggregate amount of funds in the entity’s accounts with Treasury for which the entity is authorized to make expenditures and pay liabilities.” See Appendix C for more information on FBWT. See Appendix D for a glossary of FBWT terminology.

**DoD Reporting of Receipts and Disbursements to Treasury.** Disbursing officers and agencies report their accountability and transactions on the following Standard Forms (SF):

- SF 1219: Statement of Accountability, and
- SF 1220: Statement of Transactions.

The SF 1219, Statement of Accountability, summarizes collection and disbursement activity for the month. The SF 1220, Statement of Transactions, shows a detailed account classification of the collections and disbursements processed in disbursing officers’ accounts for the current accounting period. Agencies must identify each receipt or disbursement accounting transaction with the appropriate Treasury fund account symbol.

Fund account symbols are used for internal and external reporting purposes. In general, the fund account symbol indicates (1) the department to which funds were appropriated; (2) the fiscal year(s) during which the appropriation is available for obligation; and (3) the basic fund group and numerical identification

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of the appropriation. The SF 1219 Statement of Accountability and the SF 1220 Statement of Transactions reflect the Government's receipts and disbursements. The U. S. Treasury (Treasury) uses agencies' reporting of receipts and disbursements to update its record of agencies' FBWT account balances. See Appendix E for a detailed explanation of Treasury fund symbols and expenditure and receipt accounts.

**Treasury Reports.** Treasury records the disbursement and collection data from the Statements of Transactions in the FBWT account maintained for each expenditure and receipt account in the Treasury's accounting and reporting system. The Treasury then prepares five FBWT reports including two for expenditure accounts and three for receipt accounts. See Appendix F for a discussion of the Treasury reports for FBWT.

**Reconciliation of Expenditure and Receipt Accounts.** Treasury criteria state that reconciling FBWT accounts is a key internal control process. It assures the reliability of the Government's receipt and disbursement data reported by agencies. Unresolved differences compromise the reliability of FBWT balances (as well as other Standard General Ledger balances) and Treasury's published financial reports. This, in turn, compromises the overall integrity and status of the Government's financial position. Therefore, agencies must perform timely reconciliations and implement effective and efficient reconciliation processes.

**Defense Finance and Accounting Service.** The Defense Finance and Accounting Service (DFAS) provides finance and accounting services for DoD Components. DFAS Denver performs the centralized financial accounting and reporting for the Air Force. DFAS Denver accounts for the Air Force General and Working Capital Funds.

**Defense Finance and Accounting Service Denver Financial Systems.** DFAS Denver General Accounting and Finance System–Base Level (GAFS-BL) is the standard base-level accounting and finance system used to record base level accounting transactions. GAFS-BL records all stages of fund execution, from commitment through paid accrued expenditures. Base level financial information from the GAFS-BL is electronically submitted to the General Accounting and Finance System–Rehost (GAFS-R) at DFAS Denver for processing.

GAFS-R is the official DFAS Denver accounting system for Air Force and was implemented in FY 2004. DFAS Denver uses the GAFS-R to assist in the preparation of General Fund budget reports and financial statements. Financial data flow into GAFS-R from GAFS-BL and 17 other systems.

DFAS Denver transmitted the GAFS-R beginning of period file to the Defense Departmental Reporting System–Budgetary (DDRS-B) in October 2004 to establish the beginning balances for the General Fund in DDRS-B. Each month DFAS Denver transmits the current month transaction file to DDRS-B. The current month transaction file overwrites and replaces the previous month transaction file.

**Defense Departmental Reporting System.** The Defense Departmental Reporting System (DDRS) consists of DDRS-B and DDRS-Audited Financial Statements (DDRS-AFS). DDRS-B is designed to standardize the DoD departmental reporting process and produce the monthly departmental budgetary



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reports based on the United States Standard General Ledger and standard attributes. DDRS-AFS is designed to standardize the DoD departmental financial reporting process and produce the annual and quarterly departmental reports based on the United States Standard General Ledger.

## Objectives

Our overall audit objective was to assess the controls over the FBWT account related to the General Fund financial statements for the fiscal year ending September 30, 2004. Specifically, we assessed the controls over the compilation process from the DFAS Denver GAFS-R trial balance to the published General Fund financial statements. We were not engaged to perform, and did not perform, an examination of the subject matter, the objective of which would be the expression of an opinion. We also reviewed the management control program as it related to the overall objective.

## Management Control Program Review

DoD Directive 5010.38, "Management Control (MC) Program," August 26, 1996, and DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996, require 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 the Review of the Management Control Program.** We reviewed the adequacy of DFAS Denver's internal controls over the compilation process of the General Fund FBWT account from the DFAS Denver GAFS-R trial balance to the published General Fund financial statements for FY 2004. Specifically, we reviewed DFAS Denver internal controls over the reconciliation of expenditure and receipt accounts, for classifying expenditure and receipt accounts as entity or non-entity and by fund type, for providing supporting documentation to journal voucher adjustments, and for calculating Line 2.A., "Fund Balance per Treasury," in Note 3, "Fund Balance With Treasury." We reviewed management's self-evaluation applicable to those controls.

**Adequacy of Management Controls.** We identified material management control weaknesses at the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer (OUSD[C]/CFO) and DFAS Denver as defined by DoD Instruction 5010.40. OUSD(C)/CFO and DFAS Denver internal controls over the reconciliation of expenditure and receipt accounts were not adequate to ensure that all expenditure and receipt accounts established and reported by Treasury were reconciled (finding A). Recommendation A.1., if implemented, will improve reconciliation procedures for all applicable DoD Components, and Recommendation A.2., if implemented, will further improve the reconciliation process at DFAS Denver.

In addition, OUSD(C)/CFO and DFAS internal controls were not adequate to ensure that expenditure accounts were properly assigned entity or non-entity and fund type attributes (finding B). Recommendation B.1., if implemented, will

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improve the process for assigning entity or non-entity and fund type attributes to expenditure accounts for all applicable DoD Components, and Recommendation B.2, if implemented, will further improve the process at DFAS Denver.

Also, OUSD(C)/CFO and DFAS Denver internal controls for providing supporting documentation to journal voucher adjustments were not adequate (finding C). Recommendation C.1., if implemented, will improve the procedures for providing supporting documentation to journal voucher adjustments for all applicable DoD Components, and Recommendation C.2., if implemented, will further improve the procedures at DFAS Denver.

Finally, OUSD(C)/CFO and DFAS Denver internal controls for calculating Line 2.A., "Fund Balance per Treasury," in Note 3, "Fund Balance With Treasury," were not adequate to ensure the amount was calculated correctly (finding D). Recommendation D.1., if implemented, will improve the procedures for calculating Line 2.A., "Fund Balance per Treasury," for all applicable DoD Components, and Recommendation D.2., if implemented, will further improve the procedures at DFAS Denver.

A copy of the report will be sent to the senior officials in charge of internal controls for the OUSD(C)/CFO and DFAS Denver.

**Adequacy of Management's Self-Evaluation.** DFAS Denver officials did not identify reconciling expenditure and receipt accounts, classifying expenditure and receipt accounts as entity or non-entity and by fund type, providing supporting documentation to journal voucher adjustments, and calculating Line 2.A., "Fund Balance per Treasury," in Note 3, "Fund Balance With Treasury," within its assessable units and, therefore, did not identify or report the material management control weaknesses identified by the audit.

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## A. Reconciliation of the Air Force General Fund Expenditure and Receipt Accounts

DFAS Denver did not adequately reconcile General Fund expenditure and receipt accounts to expenditure and receipt accounts established and reported in Treasury reports. Specifically, DFAS Denver did not reconcile 113 (34 percent) of the 329 expenditure and receipt accounts established and reported by Treasury as of September 30, 2004. Of the 113 expenditure and receipt accounts not reconciled:

- 59 accounts were active at least once,
- 54 accounts never had activity,<sup>1</sup> and
- 12 of the 59 accounts had activity during FY 2004 of \$10.9 billion (absolute).<sup>2,3</sup>

The inadequate reconciliation occurred because DoD criteria did not adequately implement Treasury reconciliation requirements. As a result, these unresolved differences compromised the reliability of the accounting records for DFAS Denver expenditure and receipt accounts. In addition, the lack of reconciliation further hinders preparation of General Fund auditable financial statements.

### Criteria for Reconciling Expenditure and Receipt Accounts

The Treasury Financial Management Services (FMS), through the Treasury Financial Manual (TFM), requires Federal agencies (agencies) to reconcile their FBWT expenditure and receipt accounts on a monthly basis. The OUSD(C)/CFO implements Treasury policy and DoD policy through DoD Regulation 7000.14-R, Financial Management Regulation (FMR) and interim policies and guidance promulgated through memoranda. The DFAS centers implement DoD policy through operating instructions and standard operating procedures.

**Treasury Financial Manual.** The TFM, Volume 1, Part 2, Chapter 5100, Supplement, “Fund Balance With Treasury Reconciliation Procedures,” November 1999, requires agencies to reconcile their standard general ledger account 1010, “Fund Balance With Treasury,” and any related subaccounts with the FMS 6652, 6653, 6654, and 6655 on a monthly basis (at minimum). Agencies

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<sup>1</sup>19 of the 54 accounts were FY 2005 accounts, which were established by Treasury prior to the end of FY 2004.

<sup>2</sup>The absolute total represents the absolute value when summing all lines in each monthly Treasury report. However, each line in the Treasury reports only represents the net transaction total for that line. For example, the net disbursement line may consist of a \$100 disbursement and a \$50 collection or correction for a net disbursement total of \$50. Therefore, the net disbursement totals on Treasury reports do not represent the absolute dollar amount of transactions.

<sup>3</sup>The remaining 47 accounts had activity in FY 2003 or earlier.

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must review those accounts each month to maintain the accuracy and reliability of their FBWT records for both prior year and current year appropriations. Agencies must reconcile no-year, revolving, deposit, and trust fund accounts. Agencies also must reconcile clearing and receipt accounts. This detailed reconciliation assures that agency data accumulated in the FBWT account is accurate. It also allows the agency to resolve differences in a timely manner. When resolving differences, agencies should maintain detailed reconciliation worksheets that, if needed, can be reviewed by the agency's auditors or Treasury.

**DoD Financial Management Regulations.** DoD FMR, Volume 4, Chapter 2, "Accounting for Cash and Fund Balance With Treasury," January 1995, prescribes the accounting policy and related management requirements necessary to establish financial control over FBWT and cash resources not part of the FBWT. Furthermore, Chapter 2 requires DoD to explain any discrepancies between FBWT in their general ledger accounts and the balance in the Treasury's accounts and explain the causes. Discrepancies caused by time lag should be reconciled and discrepancies caused by error should be corrected.

**DoD Memorandum.** The OUSD(C)/CFO memorandum, "Disbursement and Collection Reconciliation Procedures," February 11, 2002, requires DFAS to reconcile disbursement and collection amounts reported in the FBWT account at the DFAS center-level within 10 workdays after month-end. DFAS centers are to forward the results of the reconciliation to the OUSD(C)/CFO by the 20th working day after month-end. DFAS is to take steps to standardize best business practices within its centers to ensure the consistent application of the processes and reporting formats.

**DFAS Denver Operating Instruction.** DFAS Denver Operating Instruction 17, "Fund Balance With Treasury: Reconciliation Between Departmental Reporting Centers and Treasury Disbursements and Collections," November 1, 2003, requires DFAS Denver to compare Treasury ending account balances for the Air Force to the ending account balance for account 1010, "FBWT," in the GAFS-R. DFAS Denver is then required to research and resolve any differences by appropriation and year.

## **Reconciliation of the Air Force General Fund Expenditure and Receipt Accounts**

DFAS Denver did not adequately reconcile General Fund expenditure and receipt accounts to Treasury reports. Specifically, DFAS Denver did not reconcile 113 (34 percent) of the 329 expenditure and receipt accounts established and reported by Treasury as of September 30, 2004. Of the 113 expenditure and receipt accounts not reconciled:

- 59 accounts have been active at least once,
- 54 accounts never had activity, and
- 12 of the 59 accounts had activity during FY 2004 of \$10.9 billion (absolute).

Table 2 shows the 12 expenditure and receipt accounts that had activity during FY 2004.

**Table 2. Expenditure and Receipt Accounts with Activity for FY 2004**

<u>Account Type</u>	<u>Treasury Index</u>	<u>Fiscal Year</u>	<u>Account Number</u>	<u>Absolute Dollar Amount</u>
Expenditure	57	00	3300	\$ 383.42
Expenditure	57	F*	3875.001	8,673,411,337.23
Expenditure	57	F*	3885.007	2,233,056,987.88
Receipt	57	-	1060	332,915.91
Receipt	57	-	1099	385,728.79
Receipt	57	-	1210	5,200.00
Receipt	57	-	1299	1,191.46
Receipt	57	-	1435	2,388.49
Receipt	57	-	3200	36,826,072.78
Receipt	57	-	5095.001	920,045.33
Receipt	57	-	8928.001	2,170,369.50
Receipt	57	-	8928.002	30,302.59
<b>Total</b>				<b>\$10,947,142,923.38</b>

\*The “F” symbolizes a clearing account. See Appendix E for more information on Treasury fund symbols.

The three expenditure accounts represented 99.6 percent of the FY 2004 activity total. As of September 30, 2004, Treasury reported an ending balance of \$40.7 million for the nine receipt accounts before being closed by Treasury. The three expenditure accounts had an ending balance of (\$8.1) million.

See Appendix G for a complete list of the 113 expenditure and receipt accounts that were not reconciled by DFAS Denver. In addition, see Appendix G for the expenditure and receipt accounts that had activity at least once, that never had activity, that had activity in FY 2004, and that had a FY 2004 year-end balance.

## Adequacy of DoD Criteria

DFAS Denver did not adequately reconcile General Fund expenditure and receipt accounts to Treasury reports because the DoD criteria did not adequately implement Treasury reconciliation requirements. Specifically, the DoD FMR, OUSD(C)/CFO interim guidance, and DFAS Denver Operating Instruction did not:

- list the specific Treasury reports that DFAS should use to reconcile their expenditure and receipt accounts on a monthly basis,

- 
- require DFAS to review all the expenditure and receipt accounts reported on Treasury reports to determine whether they are valid accounts and are still being used by DFAS, and
  - require DFAS to coordinate with Treasury to remove invalid and unused expenditure and receipt accounts from Treasury reports.

In addition, the DoD FMR and OUSD(C)/CFO guidance did not require DFAS to reconcile expenditure and receipt accounts to Treasury reports on a monthly basis. Additionally, the DoD FMR and DFAS Denver Operating Instruction did not provide a time period for reconciling the expenditure and receipt accounts and reporting the reconciliation to the OUSD(C)/CFO. Also, the DFAS Denver Operating Instruction was not signed.

OUSD(C)/CFO needs to revise the DoD FMR for reconciling expenditure and receipt accounts to Treasury reports. DFAS Denver needs to delete the old Air Force Operating Instruction and develop formal standard operating procedures for reconciling expenditure and receipt accounts to Treasury reports. DFAS Denver then needs to make these procedures part of their standard operating procedures.

## **Conclusion**

Ineffective FBWT reconciliations further hinder preparation of agency auditable financial statements. Without effective agency reconciliations of receipt and disbursement activity, the agency FBWT balance—the amount of funds available to it for expenditure in each appropriation—may contain material misstatements. Generally, auditors would be unable to determine whether FBWT is fairly stated.

## **Recommendations, Management Comments, and Audit Response**

**A.1. We recommend that the Under Secretary of Defense (Comptroller)/Chief Financial Officer implement Treasury requirements by revising DoD Regulation 7000.14-R, Financial Management Regulation, Volume 4, Chapter 2, “Accounting for Cash and Fund Balance With Treasury,” issued January 1995, to establish specific procedures for the reconciliation of Fund Balance With Treasury to:**

**a. Reconcile the DoD standard general ledger account 1010, “Fund Balance With Treasury,” to the expenditure and receipt accounts listed on the following Treasury reports:**

- (1) FMS 6653, “Undisbursed Appropriation Account Ledger.”**
- (2) FMS 6654, “Undisbursed Appropriation Account Trial Balance.”**
- (3) FMS 6655, “Receipt Account Ledger.”**

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**(4) FMS 6655, “Receipt Account Trial Balance.”**

**(5) FMS 6655, “Report of Unavailable Receipt Transactions.”**

**b. Reconcile expenditure and receipt accounts on a monthly basis.**

**c. Perform the reconciliation within a specified number of days after month-end.**

**d. Report the results of the reconciliation within a specified number of days to the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer.**

**e. Review on a periodic basis, at least annually, all the expenditure and receipt accounts reported on Treasury reports to determine whether they are valid accounts and are still being used by Defense Finance and Accounting Service.**

**f. Coordinate with Treasury to remove invalid or unused expenditure and receipt accounts from Treasury reports.**

**Management Comments.** The Deputy Chief Financial Officer concurred. The Deputy Chief Financial Officer stated that the DoD FMR will be revised to state that the United States Standard General Ledger account 1010, “FBWT,” must be reconciled with the applicable Treasury reports or the Account Summary Report in the Treasury Government-Wide Accounting System. In addition, the Deputy Chief Financial Officer stated the DoD FMR will be revised to include the frequency and timeliness of the reconciliation and require an annual validation by DFAS of the DoD accounts reported in the applicable Treasury reports or the Account Summary Report. Finally, the Deputy Chief Financial Officer stated that she will not list the specific requirements in the DoD FMR, but the DoD FMR will direct the reader to Treasury FBWT reconciliation procedures.

**Audit Response.** Although the Deputy Chief Financial Officer concurred with the recommendations, we consider the comments partially responsive. We request that the Deputy Chief Financial Officer reconsider her position that specific reconciliation procedures will not be included in the DoD FMR. The DoD FMR outlines internal control requirements to ensure that DoD policy is implemented and followed. Individuals responsible for reconciling FBWT accounts need all these requirements in one location. In addition, the Deputy Chief Financial Officer did not comment on the recommendations regarding the reporting of reconciliation results and coordinating with Treasury to remove invalid or unused expenditure and receipt accounts from Treasury reports (Recommendations A.1.d. and A.1.f.). We request the Deputy Chief Financial Officer provide additional comments and an estimated completion date on the final report.

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**A.2. We recommend that the Director of Defense Finance and Accounting Service Denver:**

**a. Determine whether the 113 expenditure and receipt accounts not reconciled are valid and are still being used by the Air Force General Fund.**

**(1) If an account is valid and still being used by the Air Force General Fund, establish the expenditure or receipt account in the General Accounting and Finance System-Rehost.**

**(2) If an account is invalid and not being used by the Air Force General Fund, coordinate with Treasury to have the expenditure or receipt account removed from Treasury reports.**

**Management Comments.** The Director of DFAS Headquarters concurred. The Director stated that none of the 113 expenditure and receipt accounts identified had a material effect on the FY 2004 financial statement data. However, the following corrective actions were taken. In July 2005, Treasury removed 70 invalid accounts with zero balances as requested by DFAS Denver. In addition, DFAS Denver has taken corrective actions to establish receipt accounts in GAFS-R to facilitate the inclusion of receipt accounts in their monthly reconciliations. Additionally, DFAS Denver will include valid expenditure and suspense accounts with zero balances on their monthly reconciliations. The estimated completion date for the corrective actions was November 30, 2005.

**b. Delete Operating Instruction 17, "Fund Balance With Treasury: Reconciliation Between Departmental Reporting Centers and Treasury Disbursements and Collections," November 1, 2003.**

**Management Comments.** The Director of DFAS Headquarters concurred. The Director stated that Operating Instruction 17, "Fund Balance With Treasury: Reconciliation Between Departmental Reporting Centers and Treasury Disbursements and Collections," November 1, 2003, has been rescinded.

**c. Establish formal standard operating procedures to implement the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer requirements for reconciling expenditure and receipt accounts by establishing procedures for:**

**(1) Identifying the specific Treasury reports that Defense Finance and Accounting Service Denver should use to reconcile their expenditure and receipt accounts on a monthly basis.**

**(2) Requiring Defense Finance and Accounting Service Denver to review all the expenditure and receipt accounts reported on Treasury reports to determine whether they are valid accounts and are still being used for the Air Force General Fund.**

**(3) Requiring Defense Finance and Accounting Service Denver to establish valid accounts and accounts that are still being used by the Air Force General Fund in the Defense Finance and Accounting Service Denver General Accounting and Finance System-Rehost.**



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**(4) Requiring Defense Finance and Accounting Service Denver to coordinate with Treasury to remove from Treasury accounts the invalid accounts or accounts that are not being used by the Air Force General Fund.**

**(5) Establishing time periods for reconciling expenditure and receipt accounts and reporting the results of the reconciliation, based on policy established by the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer.**

**(6) Requiring the appropriate signature on the standard operating procedures and making these procedures part of the Defense Finance and Accounting Service standard operating procedures.**

**Management Comments.** The Director of DFAS Headquarters concurred. The Director stated that standard operating procedures are being formalized and will be updated in accordance with revised DoD Regulation 7000.14-R, FMR, Volume 4, Chapter 2, "Accounting for Cash and Fund Balance With Treasury," January 1995, and any other interim guidance provided by the OUSD(C)/CFO. The estimated completion date for the corrective actions is December 31, 2005.

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## B. Expenditure Account Attributes

DFAS Denver did not have adequate internal controls for classifying expenditure accounts as entity or non-entity and by fund type. Specifically, DFAS Denver had to create multiple journal voucher adjustments after fiscal year-end in DDRS-AFS to classify expenditure accounts as entity or non-entity and by fund type. In particular, DFAS Denver made:

- three journal voucher adjustments to assign the entity attribute and
- five journal voucher adjustments to assign the fund type attribute.<sup>4</sup>

Although the net effect of these journal voucher adjustments to the General Fund, FBWT account was \$79.3 million, a potential misclassification error of \$1.3 billion (absolute) may occur on the classification of expenditure accounts as entity or non-entity and by fund type. DFAS Denver personnel made the multiple journal voucher adjustments because DoD FMR and the OUSD(C)/CFO interim guidance did not provide adequate guidance for classifying expenditure accounts as entity or non-entity and by fund type. In addition, GAFS-R did not properly capture attributes for classifying expenditure accounts as entity or non-entity and by fund type. As a result, potential misstatements may occur on the financial statements. In addition, auditors were not able to perform a timely review of the General Fund financial statement compilation process; therefore, future audits of the General Fund financial statements may not be completed in the required 45-day timeframe.<sup>5</sup>

### Criteria

**Entity and Non-Entity Attribute.** Statement of Federal Financial Accounting Standards No. 1, “Accounting for Selected Assets and Liabilities,” March 30, 1993, states the following:

Entity assets are those assets which the reporting entity has authority to use in its operations. “Non-entity” assets are those assets that are held by an entity but are not available to the entity. ... Both entity assets and non-entity assets under an entity’s custody or management should be reported in the entity’s financial statements. Non-entity assets reported in the entity’s financial statements should be segregated from entity assets.

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<sup>4</sup>The eight journal voucher adjustments created to assign attributes were unsupported. See finding C for a further discussion of why they were unsupported.

<sup>5</sup>November 15 is the annual deadline for the DoD Agency-Wide financial statements. Therefore, General Fund FBWT auditors will have less than 45 days from September 30 to November 15 to perform their audit work.

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Office of Management and Budget (OMB) Bulletin 01-09, “Form and Content of Agency Financial Statements,” September 25, 2001, states: “To the extent that the reporting entity maintains fund balances in deposit, suspense, and clearing accounts that are not available to finance the entity’s activities, those balances should be disclosed as non-entity assets.”

DoD FMR, Volume 6B, Chapter 10, “Notes to the Financial Statements,” January 2002, Section 1004, “Note 2. Non-Entity and Entity Assets,” provides the note format for reporting entity and non-entity asset information in the notes to the financial statements. Chapter 10 also states that Appendix C provides the crosswalk to the Balance Sheet and includes the attributes to separately identify entity and non-entity amounts by the U.S. Standard General Ledger for “Note 2. Non-Entity and Entity Assets.”

DoD FMR, Volume 6B, Appendix C, “General Ledger Crosswalk for the Balance Sheet Statement,” November 2001, shows that the FBWT account can be reported as either entity or non-entity.

DoD FMR, Volume 6B, Appendix A, “Appropriation and Fund Symbols List by Reporting Entity,” November 2001, contains a list of General Fund expenditure accounts and classifies them as entity or non-entity. In addition, Appendix A classifies clearing accounts and deposit funds as non-entity accounts.

**Fund Type Attribute.** OMB Bulletin 01-09, “Form and Content of Agency Financial Statements,” September 25, 2001, provides guidance on the content of agency financial statements and notes. Specifically, the OMB guidance requires that agencies report FBWT in the notes to the financial statements in the following categories:

- Appropriated Funds,
- Revolving Funds,
- Trust Funds, and
- Other Fund Types.

DoD FMR, Volume 6B, Chapter 10, “Notes to the Financial Statements,” January 2002, Section 1005, “Note 3. Fund Balance With Treasury,” states: “... disclose the assets by fund type (appropriated, revolving, trust, or in the other fund type category). ...”

## **Audit Tools for Reviewing Financial Systems**

**GAO Guidance.** GAO-05-225G, “Checklist for Reviewing Systems under the Federal Financial Management Improvement Act,” February 2005, states: “The core financial system should provide the capability to support the following fund characteristics: fund type, such as general fund, deposit fund, trust fund, special fund, revolving fund, or receipt account.” See Appendix H for more information on the GAO Checklist.

**DFAS Guidance.** DFAS created DFAS 7900.4G, “A Guide to Federal Requirements for Financial Management Systems,” Version 4.1.2, November 2004, as a tool to focus management’s attention on the requirements financial systems must satisfy. This guide is commonly referred to by DFAS as the “Blue Book.” The Blue Book states, “The system must distinguish between entity and non-entity assets.” The Blue Book also states, at a minimum, fund type characteristics, such as general fund, deposit fund, trust fund, special fund, revolving fund, or receipt account, must be supported in accordance with Treasury and OMB reporting requirements. In addition, the Blue Book states, “The system must provide the capability to automatically generate fiscal yearend pre-closing and closing entries as they relate to fund types.” See Appendix H for more information on the DFAS Blue Book.

## Classifying Expenditure Accounts as Entity or Non-Entity

DFAS Denver created multiple journal voucher adjustments in DDRS-AFS to classify expenditure accounts with entity or non-entity attributes. The journal voucher adjustments were necessary to classify General Fund expenditure accounts as entity or non-entity for the September 30, 2004, financial statements. Specifically, DFAS Denver made three journal voucher adjustments to assign the entity attribute. Although the net effect of these journal voucher adjustments to the General Fund, FBWT account was \$79.3 million, a potential misclassification error of \$827.9 million (absolute) may occur on the classification of expenditure accounts as entity or non-entity as shown in Table 3.

<u>Journal Voucher</u>	<u>Entity Attribute</u>	<u>Debit Amount</u>	<u>Credit Amount</u>	<u>Absolute Amount</u>
27595	Non-Entity	\$ 36,826,072.78	-	\$ 36,826,072.78
27981	Entity	379,972,330.89	-	379,972,330.89
	Non-Entity	-	\$337,494,929.15	337,494,929.15
28073	Entity	36,826,072.78	-	36,826,072.78
	Non-Entity	-	36,826,072.78	36,826,072.78
<b>Total</b>		<b>\$453,624,476.45</b>	<b>\$374,321,001.93</b>	<b>\$827,945,478.38</b>

These multiple journal voucher adjustments were made because of inadequate DoD FMR and OUSD(C)/CFO interim guidance and the inability of the GAFS-R to properly capture and assign entity or non-entity attributes to expenditure accounts. For example, journal voucher 28073 was made to reverse journal voucher 27595. None of the journal voucher adjustments were supported with proper documentation.

## Classifying Expenditure Accounts by Fund Type Attribute

DFAS Denver created multiple journal voucher adjustments in DDFS-AFS to classify expenditure accounts by fund type. The journal vouchers were necessary to classify the General Fund expenditure account by fund type for the September 30, 2004, financial statements. Specifically, DFAS Denver made five journal voucher adjustments to assign the fund type attribute. Although the net effect of these journal voucher adjustments to the General Fund, FBWT account was zero, a potential misclassification error of \$422.3 million (absolute) may occur on the classification of expenditure accounts by fund type as shown in Table 4.

**Table 4. Journal Voucher Adjustments to Classify Expenditure Accounts by Fund Type**

<u>Journal Voucher</u>	<u>Fund Type Attribute</u>	<u>Debit Amount</u>	<u>Credit Amount</u>	<u>Absolute Amount</u>
27901	Appropriated Funds	-	\$ 63,101,694.87	\$ 63,101,694.87
	Other Funds	\$ 53,290,050.33	-	53,290,050.33
	Trust Funds	9,811,644.54	-	9,811,644.54
28014	Appropriated Funds	63,101,694.87	-	63,101,694.87
	Other Funds	-	53,290,050.33	53,290,050.33
	Trust Funds	-	9,811,644.54	9,811,644.54
28019	Appropriated Funds	-	63,101,694.87	63,101,694.87
	Other Funds	53,290,050.33	-	53,290,050.33
	Trust Funds	9,811,644.54	-	9,811,644.54
28552	Appropriated Funds	599,707.23	-	599,707.23
	Trust Funds	-	599,707.23	599,707.23
28556	Appropriated Funds	21,238,700.87	-	21,238,700.87
	Other Funds	-	21,238,700.87	21,238,700.87
<b>Total</b>		<b>\$211,143,492.71</b>	<b>\$211,143,492.71</b>	<b>\$422,286,985.42</b>

These multiple journal voucher adjustments occurred because of inadequate DoD FMR and OUSD(C)/CFO interim guidance and the inability of the GAFS-R to properly capture and assign fund type attributes to expenditure accounts. For example, journal voucher 27901 was made to assign fund types to expenditure accounts. Journal voucher 28014 was made to reverse journal voucher 27901 because it was incorrect, and journal voucher 28019 was made to assign the proper fund types to expenditure accounts. Journal vouchers 28552 and 28556 were made to correct journal voucher 28019. None of the journal voucher adjustments were supported with proper documentation. Finding C explains why these journal vouchers were not properly supported.

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## Adequacy of DoD Criteria for Classifying Expenditure Accounts as Entity or Non-Entity and by Fund Type

The DoD FMR and the OUSD(C)/CFO interim guidance did not provide adequate guidance for classifying expenditure accounts as entity or non-entity and by fund type.

**DoD FMR.** The DoD FMR did not adequately reference needed information in other parts of the DoD FMR, contained an incomplete list of General Fund expenditure accounts, and did not provide guidance on how to classify expenditure accounts by fund type. Specifically, the DoD FMR contained the following problems:

**Entity and Non-entity.** DoD FMR, Volume 6B, Chapter 10, “Notes to the Financial Statements,” January 2002, Section 1004, “Note 2. Non-Entity and Entity Assets,” states that Appendix C provides the crosswalk to the Balance Sheet and includes the attributes to separately identify entity and non-entity amounts by the U.S. Standard General Ledger. However, DoD FMR, Volume 6B, Appendix C, “General Ledger Crosswalk for the Balance Sheet Statement,” November 2001, only states that the FBWT account can be reported as either entity or non-entity. Specifically, Section 1004 did not reference DoD FMR, Volume 6B, Appendix A, “Appropriation and Fund Symbols List by Reporting Entity,” November 2001, which contains an incomplete list of General Fund expenditure accounts. Specifically, Appendix A did not classify 13 expenditure accounts as entity or non-entity that were listed on Treasury reports for the General Fund as of September 30, 2004. Thus, DFAS Denver did not have adequate information to classify 13 expenditure accounts as entity or non-entity.

**Fund Type.** DoD FMR, Volume 6B, Chapter 10, “Notes to the Financial Statements,” January 2002, Section 1005, “Note 3. Fund Balance With Treasury,” states: “... disclose the assets by fund type (appropriated, revolving, trust, or in the other fund type category). ...” Specifically, the General Fund FBWT account has to be classified as appropriated, trust, and other fund type. However, the DoD FMR does not provide any guidance to classify expenditure accounts by fund type.

OUSD(C)/CFO personnel stated that the DoD FMR Volume 6B was in the process of being revised and was not being followed. However, OUSD(C)/CFO did not issue any interim guidance until after the start of our audit.

**Interim Guidance.** Based on our audit work, the OUSD(C)/CFO recognized that inadequate guidance existed in the DoD FMR and on April 8, 2005, issued interim guidance to DFAS reporting centers. However, this interim guidance is inadequate for classifying expenditure accounts as entity or non-entity and by fund type.

**Entity and Non-entity.** The interim guidance did not classify nine expenditure accounts that were listed on Treasury reports for the General Fund as of September 30, 2004. The nine expenditure accounts are:

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57X1997, 57X1998, 57\*6060, 57X6275, 57X6276, 57X6500, 57X6501, 57F0109, and 57F0152.

In addition, the interim guidance instructs accountants to classify 10 clearing accounts as an entity asset. The 10 clearing accounts are: 57F3845, 57F3875, 57F3875.001, 57F3875.002, 57F3875.003, 57F3875.004, 57F3875.005, 57F3880, 57F3885, and 57F3885.007. However, this guidance conflicts with OMB Bulletin 01-09, "Form and Content of Agency Financial Statements," September 25, 2001, and the DoD FMR, Volume 6B, Appendix A, "Appropriation and Fund Symbols List by Reporting Entity," November 2001, which instructs accountants to classify expenditure clearing accounts as non-entity assets.

**Fund Type.** The interim guidance classifies receipt accounts as "Other Fund Types." Receipt accounts should not be included as part of FBWT (as discussed in finding D).

If the DoD FMR had adequate guidance, this would reduce the risk of potential misstatements and would assist auditors in performing a timely review of the General Fund FBWT account.

## General Accounting and Finance System-Rehost Limitation

GAFS-R did not properly capture attributes for classifying expenditure accounts as entity or non-entity and by fund type. Specifically, DFAS Denver personnel stated that the GAFS-R captures all expenditure accounts as "Appropriated" fund types. However, GAO-05-225G, "Checklist for Reviewing Systems under the Federal Financial Management Improvement Act," February 2005, and the Blue Book recommend that the core financial system provide the capability to capture the following fund types: general fund, deposit fund, trust fund, special fund, revolving fund, or receipt account. In addition, the Blue Book states, "The system must distinguish between entity and non-entity assets."

If the GAFS-R properly captured these attributes and had the capability to automatically generate the required year-end fund type entries, DFAS Denver would not have to make multiple journal voucher adjustments in DDRS-AFS after the fiscal year-end. This would reduce the risk of potential misstatements and would assist auditors in performing a timely review of the General Fund FBWT account.

## Conclusion

OUSD(C)/CFO needs to improve its guidance for classifying expenditure accounts as entity or non-entity and by fund type. In addition, DFAS Denver needs to modify the GAFS-R to properly capture the attributes for classifying expenditure accounts as entity or non-entity and by fund type. Classifying expenditure accounts with the proper attributes is necessary for the proper disclosure of the General Fund FBWT account. The DoD FMR requires that FBWT be segregated between entity and non-entity on the Consolidated Balance

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Sheet and in Note 2, “Non-Entity and Entity Assets.” Also, Note 3, “Fund Balance With Treasury,” requires the FBWT to be classified by fund type. Furthermore, creating multiple journal vouchers may lead to misstatements. It also requires a significant amount of time and effort by DFAS Denver personnel to process the journal voucher adjustments. This, in turn, extends the time it takes DFAS Denver to produce auditable financial statements.

## **Recommendations, Management Comments, and Audit Response**

**B.1. We recommend that the Under Secretary of Defense (Comptroller)/Chief Financial Officer provide guidance on classifying expenditure accounts as entity or non-entity and by fund type by revising:**

**a. DoD Regulation 7000.14-R, Financial Management Regulation, Volume 6B, Chapter 10, “Notes to the Financial Statements,” January 2002, to reference Volume 6B, Appendix A, “Appropriation and Fund Symbols List by Reporting Entity,” November 2001.**

**b. DoD Regulation 7000.14-R, Financial Management Regulation, Volume 6B, Appendix A, “Appropriation and Fund Symbols List by Reporting Entity,” November 2001, to include all DoD appropriation and fund symbols by reporting entity.**

**Management Comments.** The Deputy Chief Financial Officer concurred. The Deputy Chief Financial Officer stated that Volume 6B, Appendix A will be deleted. Information in Appendix A will be included in quarterly financial statement guidance posted on the OUSD(C)/CFO website and on the DFAS e-portal, including appropriations and fund symbols by reporting entity. In addition, Volume 6B, Chapter 10, will refer the reader to the OUSD(C)/CFO website.

**c. Interim guidance to classify expenditure clearing accounts as non-entity in accordance with the Office of Management and Budget Bulletin 01-09, “Form and Content of Agency Financial Statements,” September 25, 2001, and DoD Regulation 7000.14-R, Financial Management Regulation, Volume 6B, Appendix A, “Appropriation and Fund Symbols List by Reporting Entity,” November 2001.**

**Management Comments.** The Deputy Chief Financial Officer nonconcurred. The Deputy Chief Financial Officer indicated that OMB Circular A-136 and Bulletin 01-09 both state, “To the extent that the reporting entity maintains fund balance in deposit, suspense, and clearing accounts that are not available to finance the entity’s activities, those balances should be disclosed as nonentity assets.” The Deputy Chief Financial Officer also stated that the funds currently in DoD clearing accounts are available to finance the entity’s activities; therefore, they are entity accounts.

**Audit Response.** The Deputy Chief Financial Officer comments are not responsive. The Deputy Chief Financial Officer acknowledged that OMB Bulletin 01-09, “Form and Content of Agency Financial Statements,”



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September 25, 2001, and OMB Circular A-136, “Financial Reporting Requirements,” August 23, 2005, both state deposit, suspense, and clearing accounts that are not available to finance an entity’s activities should be disclosed as non-entity assets. In addition, DoD FMR, Volume 6B, Appendix A, “Appropriation and Fund Symbols List by Reporting Entity,” November 2001, instructs accountants to classify expenditure clearing accounts as non-entity assets. However, the OUSD(C)/CFO interim guidance conflicts with OMB and DoD guidance. Furthermore, this interim guidance changed OMB and DoD policy for reporting expenditure clearing accounts as non-entity assets. Therefore, we request that the Deputy Chief Financial Officer reconsider her position, provide additional comments, and provide the estimated completion date on the final report.

**d. DoD Regulation 7000.14-R, Financial Management Regulation, Volume 6B, Chapter 10, “Notes to the Financial Statements,” January 2002, Section 1005, “Note 3 Fund Balance With Treasury,” to provide guidance on how to classify expenditure accounts by fund type.**

**e. DoD Regulation 7000.14-R, Financial Management Regulation, Volume 6B, Appendix A, “Appropriation and Fund Symbols List by Reporting Entity,” November 2001, on a periodic basis, at least annually.**

**Management Comments.** The Deputy Chief Financial Officer concurred. The Deputy Chief Financial Officer stated that Volume 6B, Appendix A will be deleted. Information in Appendix A is included in the quarterly financial statement guidance posted on the OUSD(C)/CFO website and on the DFAS e-portal, including appropriations and fund symbols by reporting entity.

**Audit Response.** Although the Deputy Chief Financial Officer concurred with the recommendations, we consider the comments not responsive. The Deputy Chief Financial Officer did not address providing guidance on how to classify expenditure accounts by fund type or provide a timeframe for updating the list of appropriations and fund symbols by reporting entity. We request that the Deputy Chief Financial Officer provide additional comments on the final report. We also request the Deputy Chief Financial Officer provide the estimated completion date on the final report.

**B.2 We recommend that the Director of Defense Finance and Accounting Service Denver modify the General Accounting and Finance System-Rehost to properly capture and categorize expenditure accounts as:**

**a. Entity or non-entity.**

**Management Comments.** The Director of DFAS Headquarters concurred. The Director stated that the posting logic in GAFS-R was modified to properly categorize expenditure and receipt accounts with the proper entity or non-entity attribute. The estimated completion date for the corrective actions was November 30, 2005.

**b. The following fund types:**

**(1) General Fund**

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- (2) **Deposit Fund**
  - (3) **Trust Fund**
  - (4) **Special Fund**
  - (5) **Revolving Fund**
  - (6) **Clearing Fund**

**Management Comments.** The Director of DFAS Headquarters nonconcurred. The Director stated that the fund types are not required attributes and are in conflict with DoD FMR, Volume 6B, Chapter 10, Section 1005, “Note 3. Fund Balance With Treasury,” January 2002. Section 1005 requires the FBWT account be disclosed by the following fund types: appropriated, revolving, trust, or other.

**Audit Response.** The Director of DFAS Headquarters comments are not responsive. We agree that DoD Regulation 7000.14-R, FMR, Volume 6B, Chapter 10, Section 1005, “Note 3. Fund Balance With Treasury,” January 2002, requires that the FBWT account be disclosed by the following fund types: appropriated, revolving, trust, or other. However, we recommended that the GAFS-R be modified to properly capture and categorize expenditure accounts by fund type. Furthermore, GAO-05-225G, “Checklist for Reviewing Systems under the Federal Financial Management Improvement Act,” February 2005, requires that financial systems provide the capability to capture the fund types we recommended. We request that the Director of DFAS Headquarters reconsider his position on the recommendations and provide comments on the final report.

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## **C. DDRS-AFS Journal Voucher Adjustments**

DFAS Denver did not adequately support any of the 14 journal voucher adjustments created in DDRS-AFS to adjust the September 30, 2004, General Fund FBWT account by \$1.5 billion (absolute). This occurred because the DoD FMR did not establish adequate criteria for defining the information required to support journal voucher adjustments. Additionally, DFAS Denver did not have standard operating procedures to define what information was required to support journal voucher adjustments. As a result, potential misstatements may occur on the financial statements.

### **Criteria for Journal Vouchers**

DoD FMR, Volume 6A, Chapter 2, "Financial Reports Roles and Responsibilities," March 2002, states the following:

Proper documentation, in either hard copy or electronic form, is necessary to support all journal voucher entries. This documentation shall be sufficient for the approving official and others, such as auditors, to understand clearly the reason for preparing the journal voucher and to be able to tell it is proper and accurate.

Additionally, the DoD FMR states the following:

Adjustments made by DFAS or by DFAS Customers shall be supported by written documentation which is sufficiently detailed so that it provides audit trail to the source transaction(s) that require the adjustments. This documentation shall include the rationale and justification for the adjustment, detailed numbers and dollar amounts of errors or conditions that are related to the transaction(s) or record(s) that are proposed for adjustments, the date of the adjustment, and the name and position of the individual approving the adjustment.

### **DDRS-AFS Journal Vouchers**

DFAS Denver did not adequately support any of the 14 journal voucher adjustments created in DDRS-AFS to adjust the September 30, 2004, General Fund FBWT account by \$1.5 billion (absolute). Of the 14 unsupported journal voucher adjustments:

- 7 did not provide an adequate explanation of the reason for the journal voucher adjustment,
- 13 did not provide applicable criteria to support the explanation for the journal voucher adjustment,

- 3 did not provide a clear calculation of the dollar amount of the journal voucher adjustment, and
- 13 did not provide the specific expenditure or receipt accounts in the journal voucher that were being affected by the journal voucher adjustment.

Table 5 summarizes reasons the 14 journal voucher adjustments created in DDRS-AFS were not supported.

<b>Table 5. Unsupported September 30, 2004, General Fund, DDRS-AFS Journal Vouchers for the FBWT account</b>				
<u>Journal Voucher</u>	<u>Did Not Provide an Adequate Explanation</u>	<u>Did Not Provide Applicable Criteria</u>	<u>Did Not Provide Clear Calculation</u>	<u>Did Not Provide the Specific Expenditure or Receipt Accounts</u>
27901	X	X		X
28014	X	X		X
28019	X	X		X
28552		X		
28556		X		X
27595		X		X
28073		X		X
27594	X	X	X	X
27910			X	X
27825	X	X		X
27827	X	X		X
28334		X		X
28335		X		X
27981	X	X	X	X

The following four journal voucher adjustments (JV 28014, 28552, 28556, and 28073) were made to reverse journal voucher adjustments: JV 27901, 28019, 28019, and 27595, respectively. Therefore, DFAS Denver recognized the journal voucher adjustments were incorrect.

## Adequacy of Criteria

The DoD FMR did not establish adequate criteria for defining the information required to support journal voucher adjustments. Additionally, DFAS Denver did not have any standard operating procedures to define what information was required to support journal voucher adjustments. DFAS Denver only had draft standard operating procedures to define what information was required to support the adjustments.

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**DoD Financial Management Regulations.** The DoD FMR did not require journal voucher adjustment supporting documentation to include applicable criteria supporting the rationale for journal voucher adjustments. Additionally, the DoD FMR did not require the supporting documentation to include the specific expenditure or receipt accounts affected by journal voucher adjustments. Furthermore, the DoD FMR did not require documentation showing a clear calculation of the dollar amount for journal voucher adjustments.

**Draft Standard Operating Procedures.** DFAS Denver provided us the following draft Standard Operating Procedure (SOP), “Journal Voucher Guidance for General Funds,” December 21, 2004, which defines journal vouchers as accounting and/or adjustment entries made to the General Fund general ledger accounts. The SOP also states that journal vouchers are processed manually or mechanically through GAFS-R. Additionally, proper preparation of journal vouchers is important to ensure that documentation for detailed audit trail exists and that the journal voucher is accurately recorded as a financial event.

However, the draft SOP does not require journal voucher adjustment supporting documentation to include criteria, when applicable, to support the rationale for journal voucher adjustments. Additionally, the draft SOP does not require the supporting documentation to include the specific expenditure or receipt accounts affected by journal voucher adjustments. Furthermore, the draft SOP states that these procedures only apply to journal voucher adjustments created in GAFS-R. The draft SOP does not apply to journal voucher adjustments created in DDRS-B and DDRS-AFS. Lastly, the draft SOP does not require documentation showing a clear calculation of the dollar amount for journal voucher adjustments.

## **Conclusion**

Unsupported journal voucher adjustments may lead to potential misstatements on the General Fund financial statements and limit the ability of supervisors and auditors to substantiate the validity of the journal voucher adjustments. Additionally, we could not determine whether potential misstatements existed in the September 30, 2004, General Fund FBWT account, and we were not able to perform a timely review of the General Fund financial statement compilation process.

## **Recommendations and Management Comments**

**C.1. We recommend that the Under Secretary of Defense (Comptroller)/Chief Financial Officer enhance journal voucher documentation requirements by revising DoD Regulation 7000.14-R, Financial Management Regulation, Volume 6A, Chapter 2, “Financial Reports Roles and Responsibilities,” to require the Defense Finance and Accounting Service to provide:**

**a. Applicable criteria to support the rationale for the journal voucher adjustment on the journal voucher or supporting documentation.**

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**b. Specific expenditure or receipt accounts affected by the journal voucher adjustment on the journal voucher or supporting documentation.**

**c. Calculation of the dollar amount of the journal voucher adjustment and references to supporting documentation.**

**Management Comments.** The Deputy Chief Financial Officer concurred. The Deputy Chief Financial Officer stated that there is quarterly financial statement guidance on the OUSD(C)/CFO website with this requirement. In addition, the Deputy Chief Financial Officer stated that the requirement will be added to the DoD FMR. The Deputy Chief Financial Officer also stated that the DoD FMR will be revised to state that specific expenditure or receipt accounts must be included in the support documentation at the time the FBWT journal voucher is created. Furthermore, the Deputy Chief Financial Officer stated that the DoD FMR will be revised to include the disclosure of the calculation of the dollar amount of the adjustment within the journal voucher description or where this information can be found.

**C.2. We recommend that the Director of Defense Finance and Accounting Service Denver finalize their draft Standard Operating Procedures, “Journal Voucher Guidance for General Funds,” December 21, 2004, and make the procedures applicable to journal voucher adjustments in the Defense Departmental Reporting System-Budgetary and Defense Departmental Reporting System-Audited Financial Statements. In addition, include the following requirements to provide:**

**a. Applicable criteria to support the rationale for the journal voucher adjustment on the journal voucher or supporting documentation.**

**b. Specific expenditure or receipt accounts affected by the journal voucher adjustment on the journal voucher or supporting documentation.**

**c. Calculation of the dollar amount of the journal voucher adjustment and references to supporting documentation.**

**Management Comments.** The Director of DFAS Headquarters concurred. The Director stated that the finding was not material, and that journal voucher narrative explanations can always be improved. However, the draft standard operating procedures will be enhanced and finalized to include the following requirements: applicable criteria to support the rationale for the journal voucher adjustments on the journal voucher or supporting documentation, specific expenditure or receipt accounts affected by the journal voucher adjustment on the journal voucher or supporting documentation, and the calculation of the dollar amount of the journal voucher adjustment and references to supporting documentation. The estimated completion date was November 30, 2005.

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## D. Air Force, General Fund, Note 3, “Fund Balance With Treasury”

DFAS Denver incorrectly:

- included \$6.9 million of Air Force transfers to the Department of Transportation,
- excluded \$16.1 million of transfers to the Air Force from the OMB and the Department of Agriculture, and
- included \$152 million in unavailable receipt accounts in Line 2.A., “Fund Balance per Treasury.”

The overstatement occurred because DoD FMR did not specify which expenditure and receipt accounts should be included in the amount for Line 2.A., “Fund Balance per Treasury,” and DFAS Denver did not have standard operating procedures for calculating the amount for Line 2.A., “Fund Balance per Treasury.” Additionally, OMB guidance conflicts with Federal Accounting Standards Advisory Board (FASAB) accounting standards for reporting transfers and Treasury guidance is unclear. As a result, DFAS Denver overstated the amount for Line 2.A., “Fund Balance per Treasury,” in Note 3, “Fund Balance With Treasury,” by \$142.8 million on the September 30, 2004, General Fund financial statements. Furthermore, DFAS Denver is not reporting the correct reconciling amount in Note 3, “Fund Balance With Treasury.”

### Criteria for Reporting Transfers and Receipts, and Fund Balance With Treasury Note Disclosure Requirements

The American Institute of Certified Public Accountants designated the FASAB as the body that establishes accounting principles for Federal entities. FASAB establishes accounting principles through the Statement of Federal Financial Accounting Standards (SFFAS). Additionally, the DoD FMR, Volume 1, Chapter 8, “Hierarchy of Accounting Standards,” May 1998, sets forth the sequence of accounting standards that must be followed by DoD and its Components. Appendix I discusses the hierarchy of accounting standards.

**Federal Accounting Standards Advisory Board.** SFFAS No. 1, “Accounting for Selected Assets and Liabilities,” March 30, 1993, defines FBWT as, “... the aggregate amount of funds in the entity’s accounts with Treasury for which the entity is authorized to make expenditures and pay liabilities.”

**Transfers.** SFFAS No. 1 states that an entity’s FBWT account is increased by receiving transfers from other agencies. An entity’s FBWT is reduced by transfers to other agencies or the Treasury.

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**Receipts.** SFFAS No. 1 states an entity's FBWT account is increased by "... amounts collected and credited to appropriation or fund accounts that the entity is authorized to spend or use to offset its expenditures."

**Office of Management and Budget.** OMB Circular No. A-11, "Preparation, Submission, and Execution of the Budget," Section 20, "Terms and Concepts," July 2004, discusses transfers of budgetary resources. Specifically, the OMB Circular states that when a transfer is made from budgetary resources from one purpose to another, the parent (transferor of the appropriation) reports a transfer out. The child (recipient of the appropriation transfer) reports a transfer in. However, when a transfer is made to carry out the purposes of the parent, the activity is reported in the parent's financial statements.

OMB Bulletin 01-09, "Form and Content of Agency Financial Statements," September 25, 2001, provides guidance on the content of agency financial statements and notes. Specifically, the OMB Bulletin requires agencies in Note 3, "Fund Balance With Treasury," to explain any discrepancies between FBWT, as reflected in the entity's general ledger, and the balance in the Treasury accounts. Disclose any other information necessary for understanding the nature of FBWT.

**Treasury Financial Manual.** TFM, Volume 1, Part 2, Chapter 2000, "Warrant and Nonexpenditure Transfer (NET) Transactions," December 15, 2004, defines a nonexpenditure transfer transaction as "A transaction that does not represent payment for goods and services but serves only to adjust amounts available in accounts."

TFM, Volume 1, Part 2, Chapter 4700, "Agency Reporting Requirements for the Financial Report of the U.S. Government," May 28, 2004, states that the parent should report the activity in its financial statements, unless the allocation transfer is material to the child's financial statements. If the allocation transfer is material to the child's financial statements, the child should report the activity relating to the allocation in all of its financial statements, except the Statement of Budgetary Resources. In this case, the parent should continue to report the appropriation and the related budgetary activity in its Statement of Budgetary Resources. It is the responsibility of the parent to ensure that the reporting to Treasury is consistent with the presentation in the financial statements.

**DoD Financial Management Regulations.** DoD FMR, Volume 3, "Budget Execution-Availability and Use of Budgetary Resources," Chapter 13, "Receipt and Distribution of Budgetary Resources," December 1996, prescribes the standards for recording distribution of budgetary resources in Department-level accounts. The DoD FMR defines appropriation transfers as distributions of one agency's budgetary resources to another agency. Once the appropriation transfer is complete, the parent no longer has budgetary and proprietary control of the funds. Budgetary and proprietary responsibility now lies with the child.

**Fund Balance With Treasury Disclosure Requirements.** DoD FMR, Volume 6B, "Form and Content of the Department of Defense Audited Financial Statements," Chapter 10, "Notes to the Financial Statements," January 2002, provides guidance on the presentation of Note 3, "Fund Balance With Treasury." Specifically, the DoD FMR illustrates the format for the presentation of Note 3, "Fund Balance With Treasury," as demonstrated in Table 6.



<b>Table 6. DoD FMR Sample Format for Note 3</b>		
<b>Note 3. Fund Balance With Treasury</b>		
As of September 30,	Current FY	Prior FY
<b>1. Fund Balances:</b>		
A. Appropriated Funds	\$XXX	\$XXX
B. Revolving Funds	XXX	XXX
C. Trust Funds	XXX	XXX
D. Other Fund Types	<u>XXX</u>	<u>XXX</u>
E. Total Fund Balances	<u>\$XXX</u>	<u>\$XXX</u>
<b>2. Fund Balance Per Treasury Versus Agency:</b>		
A. Fund Balance per Treasury	\$XXX	\$XXX
B. Fund Balance per [Reporting Entity]	<u>XXX</u>	<u>XXX</u>
C. Reconciling Amount	<u>\$XXX</u>	<u>\$XXX</u>
<b>3. Explanation of Reconciliation Amount:</b>		
<b>4. Other Information Related to FBWT:</b>		

DoD FMR requires the following discussion for Lines 3 and 4 of Note 3, “Fund Balance With Treasury:”

- Line 3 should explain the cause of any reconciling amounts. Discrepancies caused by errors and timing difference should add up to the reconciling amount reported on line 2.C.
- Line 4 should explain any material fluctuations (greater than 10 percent) in the entity’s FBWT amount from the prior period, and disclose any instances where the entity does not meet accounting standards.

## **Air Force, General Fund, Note 3, “Fund Balance With Treasury,” Line 2.A., Fund Balance per Treasury**

DFAS Denver overstated the amount for Line 2.A., “Fund Balance per Treasury,” in Note 3, “Fund Balance With Treasury,” by \$142.8 million on the September 30, 2004, General Fund financial statements. Specifically, DFAS Denver, incorrectly:

- included \$6.9 million of Air Force transfers to the Department of Transportation in expenditure accounts 6957\*3300 and 6957\*3400,
- excluded \$16.1 million of transfers to the Air Force from the OMB and the Department of Agriculture in expenditure accounts 5711\*1081, 5711\*1082, 5711\*1088, and 5711\*1105, and

- 
- included \$152 million in unavailable receipt accounts.

DFAS Denver used the following methodology to calculate the amount for Line 2.A., “Fund Balance per Treasury,” of Note 3, “FBWT.” DFAS Denver:

- Included \$61,355 million from the FMS 6654, “Undisbursed Appropriation Account Trial Balance,” for the General Fund.
- Included \$6.9 million from expenditure accounts 6957\*3300 and 6957\*3400. These expenditure accounts represent funds that were transferred from the General Fund to the Department of Transportation.
- Excluded \$16.1 million from expenditure accounts 5711\*1081, 5711\*1082, 5711\*1088, and 5712\*1105. These expenditure accounts represent funds that were transferred to the General Fund from OMB and the Department of Agriculture.
- Included \$152 million from the FMS 6655, “Report of Unavailable Receipt Transactions,” for the General Fund.

This calculation resulted in an amount of \$61,497.8 million reported in Line 2.A., “Fund Balance per Treasury,” in Note 3, “Fund Balance With Treasury,” on the September 30, 2004, General Fund financial statements. DFAS Denver, by including the appropriation transfer out (\$6.9 million) and unavailable receipt accounts (\$152 million), and excluding the transfer in (\$16.1 million) for their calculation of Line 2.A., “Fund Balance per Treasury,” overstated the amount by \$142.8 million.

## **Adequacy of Criteria for Reporting Line 2.A., “Fund Balance per Treasury”**

The DoD FMR did not specify what expenditure and receipt accounts should be included in the amount for Line 2.A., “Fund Balance per Treasury.” Specifically, the DoD FMR did not state whether the parent or child should report the activity from transfers reported in expenditure accounts in their financial statements. Also, the DoD FMR did not state that receipt accounts should not be included in the amount for Line 2.A., “Fund Balance per Treasury.” In addition, DFAS Denver did not have standard operating procedures for calculating the amount for Line 2.A., “Fund Balance per Treasury.”

**Criteria for Reporting Transfers.** OMB guidance conflicts with FASAB accounting standards for reporting transfers and Treasury guidance is unclear. The following paragraph summarizes the FASAB accounting standard for reporting transfers in the FBWT account. The subsequent paragraphs discuss OMB’s conflicting guidance and Treasury’s unclear guidance.

**Financial Accounting Standards Advisory Board Criteria.** FASAB states that an entity’s FBWT account is increased by receiving transfers from other agencies. An entity’s FBWT is reduced by transfers to other entities or the Treasury. In other words, the parent would report a transfer

out, and the child would report a transfer in and report the activity in their financial statements.

**Office of Management and Budget Criteria.** OMB states that the nature of the transfer determines whether the parent or child reports the activity in their financial statements. Specifically, OMB states that when a transfer is made of budgetary resources from one purpose to another, the parent reports a transfer out and the child reports a transfer in. Thus, the child would report the activity in their financial statements. However, when a transfer is made to carry out the purposes of the parent, the activity is reported in the parent financial statements. OMB guidance contradicts FASAB accounting standards because the nature of the transaction determines whether the parent or child reports the transfer activity.

**Treasury Financial Manual Criteria.** TFM guidance is unclear because it uses the terms transfer and allocation interchangeably. However, OMB defines transfers and allocations as follows:

- A transfer reduces budgetary resources (budget authority and unobligated balances) in one account and increases them in another by the same amount.
- An allocation is a legal delegation by one agency of its authority to obligate budget authority and outlay funds to another agency.

TFM guidance may conflict with FASAB accounting standards if Chapter 4700 is providing guidance for reporting transfers. TFM states that the parent should report the activity in its financial statements, unless the transfer is material to the child's financial statements. If the transfer is material to the child's financial statements, the child should report the activity relating to the transfer in all of its financial statements, except the Statement of Budgetary Resources. TFM contradicts FASAB accounting standards because the materiality of the transfer to the child determines who reports the transfer activity.

Table 7 summarizes the criteria for reporting transfer activity on agency financial statements.

<b>Table 7. Criteria for Reporting Transfer Activity on an Agency's Financial Statements</b>		
<b>SFFAS</b>	<b>OMB</b>	<b>TFM</b>
The child reports the transfer activity in its financial statements.	The nature of the transfer determines whether the parent or child reports the transfer activity in their financial statements.	The parent reports the transfer activity in its financial statements, unless the transfer is material to the child's financial statements.

DFAS Denver should not have included the \$6.9 million of Air Force appropriations transferred to the Department of Transportation and should not have excluded \$16.1 million of appropriations transferred to the Air Force from the OMB and the Department of Agriculture.

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**Criteria for Reporting Receipt Accounts.** SFFAS No. 1 defines FBWT as the balance with Treasury for which the entity is authorized to make expenditures and pay liabilities. Thus, DFAS Denver should not have included the \$152 million from U.S. Treasury FMS 6655 “Report of Unavailable Receipt Transactions,” in Line 2.A., “Fund Balance per Treasury,” because these receipts are not available for expenditures and payment of liabilities of the General Fund. Additionally, if DFAS Denver had available receipt amounts in FMS 6655, “Receipt Account Trial Balance,” or FMS 6655, “Receipt Account Ledger,” these amounts would not be included in Line 2.A., “Fund Balance per Treasury,” because these receipts would have already been made available to General Fund by Treasury through an invisible warrant. Specifically, Treasury transfers funds from available receipt accounts to expenditure accounts through an invisible warrant.

**Hierarchy of Accounting Standards.** DoD FMR, Volume 1, Chapter 8, “Hierarchy of Accounting Standards,” May 1998, sets forth the accounting standards that shall be followed by Federal agencies, including DoD. Chapter 8 states that approved SFFASs comprise Federal generally accepted accounting principles and must be followed by DoD and each DoD Component. Additionally, DoD and its Components must adhere to the hierarchy of Federal generally accepted accounting principles in the order of precedence listed in Chapter 8. SFFASs are the first in the order of precedence listed in Chapter 8. Therefore, SFFAS No. 1 is the controlling guidance in determining which expenditure and receipt accounts should be included in the amount for Line 2.A., “Fund Balance per Treasury.”

## Conclusion

OUSD(C)/CFO needs to improve its guidance in the DoD FMR. In addition, DFAS Denver needs to develop standard operating procedures for identifying the expenditure and receipt accounts that should be used in the calculation of Line 2.A., “Fund Balance per Treasury.” Furthermore, the OUSD(C)/CFO needs to coordinate with OMB to revise the OMB guidance that conflicts with FASAB SFFAS No. 1 for reporting appropriation transfers.

The proper reporting of appropriation transfers is not only necessary for DoD and its Component financial statements; it is also necessary for other Federal agencies. The existing conflicting guidance may cause other Federal agencies to incorrectly report their reconciling amount in Note 3, “Fund Balance With Treasury,” and not properly reconcile their FBWT account. There is no impact on the Federal Government consolidated financial statements because FBWT is not reported on these financial statements. According to SFFAS No. 1,

From the reporting agency’s perspective, a fund balance with Treasury is an asset because it represents the entity’s claim to the federal government’s resources. However, from the perspective of the federal government as a whole, it is not an asset; and while it represents a commitment to make resources available to federal departments, agencies, programs, and other entities, it is not a liability.

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## Recommendations, Management Comments, and Audit Response

**D.1. We recommend that the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer:**

**a. Coordinate with the Office of Management and Budget to revise OMB Circular No. A-11, "Preparation, Submission, and Execution of the Budget," Section 20, "Terms and Concepts," July 2004, to require the recipient of the transfer to report the financial activity in their records and financial statements.**

**b. Coordinate with the U.S. Treasury to revise TFM, Volume 1, Part 2, Chapter 4700, "Agency Reporting Requirements for the Financial Report of the U.S. Government," to:**

**(1) Distinguish between transfers and allocations.**

**(2) Require the recipient of the transfer to report the financial activity in their records and financial statements.**

**Management Comments.** The Deputy Chief Financial Officer concurred. The Deputy Chief Financial Officer stated that the Form and Content Subcommittee of the Chief Financial Office Council has formed a workgroup whose goal is to investigate and propose a revised accounting treatment for allocation transfers. A member of the OUSD(C)/CFO staff chairs the workgroup.

**Audit Response.** Although the Deputy Chief Financial Officer concurred with the recommendations, we consider the comments partially responsive. The Deputy Chief Financial Officer response is unclear as to whether the Department will propose and coordinate accounting policy with OMB to require recipients of appropriation transfers report the financial activity in their records and financial statements. Additionally, the Deputy Chief Financial Officer did not state whether the Department will coordinate with Treasury to distinguish between transfers and allocation of funds, and propose and coordinate accounting policy with Treasury to require that recipients of appropriation transfers report the financial activity in their records and financial statements. We request the Deputy Chief Financial Officer provide additional comments and an estimated completion date on the final report.

**c. Revise DoD Regulation 7000.14-R, DoD Financial Management Regulation, Volume 6B, "Format of DoD Audited Financial Statements," Chapter 10, "Notes to the Financial Statements," January 2002, to:**

**(1) Establish policy for identifying the expenditure and receipt accounts that should be used in the calculation of Line 2.A., "Fund Balance per Treasury," of Note 3, "Fund Balance With Treasury."**

**(2) Incorporate the policy for identifying the expenditure and receipt accounts that should be used in the calculation of Line 2.A., "Fund Balance per Treasury," of Note 3, "Fund Balance With Treasury."**

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**Management Comments.** The Deputy Chief Financial Officer concurred. The Deputy Chief Financial Officer stated that because the expenditure and receipt accounts list changes, the information will be included in quarterly guidance posted on the OUSD(C)/CFO website and the DFAS e-portal. In addition, the DoD FMR will refer the reader to the OUSD(C)/CFO website.

**Audit Response.** The Deputy Chief Financial Officer comments are not responsive. The Deputy Chief Financial Officer response did not address recommendations to establish and incorporate policy that describes the methodologies used to identify accounts required to be reported on Line 2.A., “Fund Balance per Treasury,” of Note 3, “Fund Balance With Treasury.” We request the Deputy Chief Financial Officer provide additional comments and an estimated completion date on the final report.

**D.2. We recommend that the Director of Defense Finance and Accounting Service Denver establish standard operating procedures for identifying the expenditure and receipt accounts that should be used in the calculation of Line 2.A., “Fund Balance per Treasury,” of Note 3, “Fund Balance With Treasury.”**

**Management Comments.** The Director of DFAS Headquarters concurred. The Director stated the finding was not material and that the OUSD(C)/CFO has clarified reporting requirements for Line 2.A., “Fund Balance per Treasury,” of Note 3, “Fund Balance With Treasury.” Based on this revised guidance, DFAS will establish standard operating procedures to identify the expenditure and receipt accounts that should be used in the calculation of Line 2.A., “Fund Balance per Treasury.” The estimated completion date for these corrective actions was November 30, 2005.

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## E. DFAS Denver Management Control Program for FBWT

The DFAS Denver Management Control Program for FBWT was ineffective and did not identify and report material weaknesses for FBWT in their FY 2004 Annual Statement of Assurance.<sup>6</sup> This occurred because DFAS Denver did not adequately perform a general assessment of the internal controls for the General Fund FBWT account. Specifically, the DFAS Denver Management Control Program for FBWT did not establish specific control objectives, potential risks, and control techniques within their assessable units that would have prevented the material weaknesses from occurring. Furthermore, DFAS Denver's test of controls for reconciling the General Fund FBWT account was inadequate. As a result, DFAS Denver cannot provide reasonable assurance that internal controls for the General Fund FBWT account are in place and operating effectively.

### Criteria for Management Control Programs

**Government Accountability Office.** GAO/AIMD-00-21.3.1, "Standards for Internal Control in the Federal Government," November 1999, (The Green Book) states,

The Federal Managers' Financial Integrity Act (FMFIA) of 1982 requires GAO to issue standards for internal control in government. The standards provide the overall framework for establishing and maintaining internal control and for identifying and addressing major performance and management challenges and areas at greatest risk of fraud, waste, abuse, and mismanagement.

The five standards for internal control are: control environment, risk assessment, control activities, information and communications, and monitoring. These standards define the minimum level of quality acceptable for internal control in government and provide the basis against which internal control is to be evaluated.

**Office of Management and Budget.** OMB Circular A-123, "Management Accountability and Control," revised June 21, 1995<sup>7</sup>, provides guidance to Federal managers on improving the accountability and effectiveness of Federal programs and operations by establishing, assessing, correcting, and reporting on management controls. The OMB Circular states:

Management controls are the organization, policies, and procedures used by agencies to reasonably ensure that programs achieve their

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<sup>6</sup>See the Management Control Program Review section for a discussion of the DFAS Denver Management Control Program for findings A, B, C, and D.

<sup>7</sup>The OMB recently issued a revised OMB Circular A-123, "Management's Responsibility for Internal Control," December 21, 2004; however, this revised guidance does not take effect until FY 2006. In the interim, the previous guidance should be followed.

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intended results; resources are used consistent with agency mission; programs and resources are protected from waste, fraud, and mismanagement; laws and regulations are followed; and reliable and timely information is obtained, maintained, reported, and used for decision making.

**DoD Directive.** DoD Directive 5010.38, “Management Control (MC) Program,” August 26, 1996, implements GAO and OMB guidance that is required by the FMFIA of 1982. The DoD Directive requires DoD Components to implement a comprehensive strategy for management controls that provides reasonable assurance that “... programs and administrative and operating functions are efficiently and effectively carried out in accordance with applicable law and management policy.” The management control process should be integrated into the daily management practices of all DoD managers. When developing the Management Control Program, DoD managers should rely on all contributing information sources, including external audits.

**DoD Instruction.** DoD Instruction 5010.40, “Management Control (MC) Program Procedures,” August 28, 1996, requires DoD Components to develop a Management Control Program. The Management Control Program, through its self assessment process, assists managers in identifying material management control weaknesses. The DoD Instruction states that in order to be a material weakness, two conditions must be satisfied:

- management controls are not in place, not used, or not adequate, and
- the weakness is material enough to require the attention of the next level of management.

Each DoD Component should submit an annual statement of assurance based on a general assessment of the effectiveness of the management controls. See Appendix J for a discussion of the elements of a management control program.

## **DFAS Denver General Assessment of Internal Controls**

DFAS Denver did not adequately perform a general assessment of their internal controls for the General Fund FBWT account. Specifically, the DFAS Denver Management Control Program for FBWT did not establish specific control objectives, potential risks, and control techniques within their assessable units that would have prevented the material weaknesses from occurring. Furthermore, DFAS Denver’s test of controls for reconciling the General Fund FBWT account was inadequate.

DFAS Denver’s list of assessable units included three assessable units within DFAS Denver General Funds Departmental Reporting and Requirement Directorate that relate to the General Fund FBWT account. These assessable units were responsible for ensuring that:

- cash disbursements for DFAS Denver sites reconcile with accounting records,



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- budgetary reports and financial statements are complete and accurate and submitted by the required due date,
  - the Master Appropriation Reference Table is properly maintained and updates are timely and accurate,
  - systems meet critical user requirements and comply with legal and regulatory guidance, and
  - guidance and procedures are available and regularly updated.

One assessable unit included a control technique for reconciling FBWT with the Department On-line Accounting and Reporting System for all appropriations, but this system was replaced by GAFS-R in FY 2004. Additionally, this assessable unit included a test to validate that documentation exists to illustrate that DFAS Denver reconciles the GAFS-R to Treasury records. However, our audit shows that DFAS Denver was not adequately reconciling expenditure and receipt accounts.

Overall, these assessable units did not establish specific control objectives, potential risks, and control techniques to prevent the material weaknesses from occurring. Furthermore, two of the assessable units did not have any tests of controls and the other did not have adequate tests of controls for reconciling the General Fund FBWT account. Specifically, DFAS Denver officials did not adequately reconcile expenditure and receipt accounts (finding A), classify expenditure and receipt accounts as entity or non-entity and by fund type (finding B), provide supporting documentation to journal voucher adjustments (finding C), and calculate Line 2.A., “Fund Balance per Treasury,” in Note 3, “Fund Balance With Treasury (finding D).”

## **DFAS-Wide Material Weaknesses**

DFAS Denver is required to establish and maintain a Management Control Program to provide reasonable assurance that programs are operating as intended through their Annual Statement of Assurance (ASA). The ASA is based on a general assessment that represents DFAS Denver’s informed judgment of the overall adequacy and effectiveness of their management controls. The ASA must also include material weaknesses and the plan to correct them.

DFAS Denver, along with DFAS Cleveland and DFAS Indianapolis, submit their ASA to DFAS Headquarters annually. DFAS Headquarters then issues a consolidated ASA for DFAS to the OUSD(C)/CFO, who includes the ASA in the DoD Performance and Accountability Report. Specifically, the DFAS FY 2004 ASA was provided in the Deputy Secretary’s Message at the front of the FY 2004 Performance and Accountability Report. The Performance and Accountability Report fulfills the requirements of the FMFIA of 1982.

However, DFAS Denver did not report two DFAS-wide material weaknesses that were identified and reported in the FY 2004 DFAS Headquarters ASA and DoD Performance and Accountability Report. Specifically, the following material weaknesses were reported:

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- **Fund Balance With Treasury.** The appropriation balances recorded in DFAS accounting records do not balance to Treasury records. DoD has had long-standing problems in reconciling transaction activity in their FBWT accounts. Large unsupported differences remain that contribute to DoD's inability to prepare auditable financial statements.
  - **Suspense Accounts.** DFAS centers are unable to reconcile Treasury suspense accounts to their field offices. In addition, the DFAS centers are not aging suspense accounts in accordance with DoD criteria.

## **Recommendations, Management Comments, and Audit Response**

**E.1. We recommend that the Director of Defense Finance and Accounting Service Denver:**

**a. Develop tests to determine whether internal controls have been designed and implemented to prevent the material weaknesses identified in findings A, B, C, and D of this report.**

**b. Report the material weaknesses identified in findings A, B, C, and D of this report in their Annual Statement of Assurance until they are corrected.**

**Management Comments.** The Director of DFAS Headquarters nonconcurred. The Director stated that none of the findings were proven to identify any material or substantive deficiencies. In addition, the Director stated that there is a formal and documented internal control structure in place at DFAS Denver.

**Audit Response.** The Director of DFAS Headquarters comments are not responsive. We identified material weaknesses as defined by DoD Instruction 5010.40, "Management Control (MC) Program Procedures," August 28, 1996, for the General Fund FBWT account. Specifically, we determined that the DFAS Denver internal controls over reconciling expenditure and receipt accounts (finding A), assigning entity or non-entity and fund type attributes to expenditure accounts (finding B), providing supporting documentation to journal voucher adjustments (finding C), and calculating Line 2.A., "Fund Balance per Treasury," in Note 3, "Fund Balance With Treasury," (finding D) were not adequate. The identified material internal control weaknesses relate to the compilation and reporting of the General Fund FBWT account on the Balance Sheet. DFAS Denver concurred with all of these findings and recommendations except for Recommendations B.2.b.(1)-(6).

Our review of the DFAS Denver management control program for the General Fund FBWT account determined that DFAS Denver did not identify and report these material weaknesses in the DFAS Denver FY 2004 ASA. Therefore, DFAS Denver needs to develop tests of controls within their assessable units that will prevent these material weaknesses from occurring. We request that the Director

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of DFAS Headquarters reconsider his position on the recommendations and provide comments on the final report.

**c. Establish coordination procedures with Defense Finance and Accounting Service Headquarters to ensure consistent reporting of applicable material weaknesses between the Defense Finance and Accounting Service Denver Annual Statement of Assurance and the Defense Finance and Accounting Service Headquarters Annual Statement of Assurance.**

**Management Comments.** The Director of DFAS Headquarters nonconcurred but did not provide any further comments.

**Audit Response.** The Director of DFAS Headquarters comments are not responsive. Our audit results showed that DFAS Denver did not report two DFAS material weaknesses that were identified and reported in the DFAS Headquarters FY 2004 ASA and the DoD Performance and Accountability Report. Establishing coordination procedures will prevent future inconsistencies between DFAS Headquarters and DFAS Denver ASAs and the DoD Performance and Accountability Report. This is not only necessary for the General Fund FBWT account; it is also necessary for all other accounts. We request that the Director of DFAS Headquarters reconsider his position on the recommendation and provide comments on the final report.

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## Appendix A. Scope and Methodology

We reviewed the internal controls over the FBWT account related to the General Fund Financial Statements for the fiscal year ending September 30, 2004. Specifically, we reviewed the controls over the compilation process from the DFAS Denver GAFS-R trial balance to the published General Fund financial statements. We also reviewed the management control program as it related to the overall objective.

We compared the expenditure and receipt accounts reported on Treasury reports to the expenditure and receipt accounts reported on the General Fund GAFS-R trial balance for September 30, 2004. All Treasury expenditure and receipt accounts not reported on the GAFS-R trial balance were identified and listed. We then determined the expenditure and receipt accounts that had activity at least once, that never had activity, that had activity in FY 2004, and that had a FY 2004 year-end balance. We determined whether an expenditure or receipt account had activity based on Treasury reports. Specifically, we reviewed the following Treasury reports:

- FMS 6653, “Undisbursed Appropriation Account Ledger,”
- FMS 6654, “Undisbursed Appropriation Account Trial Balance,” and
- FMS 6655, “Receipt Account Trial Balance.”

We only calculated the expenditure and receipt account activity for FY 2004. We did not calculate the dollar amount of account activity for FY 2003 and prior years. Activity includes beginning balance, appropriations received, nonexpenditure transfers, and net disbursements. We did not review the adequacy of the reconciliation process for the expenditure and receipt accounts that agreed with Treasury reports. We did not determine the adequacy of this reconciliation process because DFAS Denver adjusts expenditure and receipt accounts reported in GAFS-R to Treasury reports. We will review this reconciliation process in a subsequent audit.

We reviewed the 14 journal voucher adjustments made by DFAS Denver in DDRS-AFS. Specifically, we reviewed these journal voucher adjustments to determine whether they were adequately supported.

We reviewed DFAS Denver methodology for calculating the amount for Line 2.A., “Fund Balance per Treasury.” We then compared their methodology to criteria from FASAB, OMB, Treasury, and the DoD FMR. We only reviewed the transfers used by DFAS Denver for their calculation of Line 2.A., “Fund Balance per Treasury.”

We did not review all the internal controls for the General Fund FBWT account. We did not perform any fieldwork at the DFAS Denver disbursing stations. In addition, we did not determine whether disbursement and collection transactions were adequately supported, properly recorded, accurately processed, and properly reported to Treasury by DFAS Denver disbursing stations. Additionally, we did not trace any disbursement or collection transactions from their source documents

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to accounting databases or the GAFS-R to determine if they were properly recorded. Also, we did not trace any transactions from their source documents to the General Fund financial statements. Furthermore, we did not perform any internal control testing of GAFS-R or any of its feeder systems.

We performed this audit from October 22, 2004, through June 14, 2005, in accordance with generally accepted government auditing standards.

**Use of Computer-Processed Data.** We relied on computer-processed data from the Treasury accounting and reporting system obtained through the Government On-Line Accounting Link Information Access System II (GOALS II). Specifically, we relied on the following September 30, 2004, Treasury reports for Fund Balance With Treasury:

- FMS 6653, “Undisbursed Appropriation Account Ledger,”
- FMS 6654, “Undisbursed Appropriation Account Trial Balance,”
- FMS 6655, “Receipt Account Ledger,”
- FMS 6655, “Receipt Account Trial Balance,” and
- FMS 6655, “Report of Unavailable Receipt Transactions.”

We compared the expenditure and receipt accounts reported by Treasury to the expenditure and receipt accounts reported on the GAFS-R trial balance as of September 30, 2004. We identified all Treasury expenditure and receipt accounts not included on the GAFS-R trial balance. We did not perform a formal reliability assessment of computer-processed financial data because GOALS II is a Treasury system and the system is outside the scope of this project and DoD (Treasury maintains the system).

We also relied on the September 30, 2004, GAFS-R trial balance. We compared the expenditure and receipt accounts reported on the GAFS-R trial balance to the expenditure and receipt accounts reported by Treasury. We did not perform a formal reliability assessment of computer-processed financial data because we are not determining the accuracy of the expenditure and receipt accounts’ balances. We did not find errors that would preclude the use of the computer-processed data to meet the audit objectives or that would change the conclusions in the report.

We also relied on data from DDRS-B. Specifically, we relied on the September 30, 2004, DDRS-B journal voucher log to determine the net and absolute dollar amount of journal voucher adjustments made in DDRS-B to the General Fund FBWT account balance. We did not perform a formal reliability assessment of computer-processed data because we were only determining whether DFAS Denver could adequately support the journal voucher adjustments. We did not find errors that would preclude the use of the computer-processed data to meet the audit objectives or that would change the conclusions in the report.

We also relied on data from DDRS-AFS. Specifically, we relied on the September 30, 2004, DDRS-AFS journal voucher log to determine the net and absolute dollar amount of journal voucher adjustments made in DDRS-AFS to the General Fund FBWT account balance. We did not perform a formal reliability

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assessment of computer-processed data because we were only determining whether DFAS Denver could adequately support the journal voucher adjustments. We did not find errors that would preclude the use of the computer-processed data to meet the audit objectives or that would change the conclusions in the report.

Additionally, we relied on the September 30, 2004, DDRS-AFS financial statements and notes. We compared them to the September 30, 2004, General Fund published financial statements and notes. Specifically, we compared DDRS-AFS Balance Sheet, FBWT line item, and Note 3, "Fund Balance With Treasury," to the information reported in the published General Fund financial statements. We did not perform a formal reliability assessment of computer-processed data because we were only verifying that the information in the DDRS-AFS financial statement and notes agreed with the published General Fund financial statements and notes. We did not find errors that would preclude the use of the computer-processed data to meet the audit objectives or that would change the conclusions in the report.

**Government Accountability Office High-Risk Area.** The Government Accountability Office has identified several high-risk areas in DoD. This report provides coverage of the Financial Management high-risk area. GAO considered DoD Financial Management a high risk because DoD's financial management deficiencies represent the single largest obstacle to achieving an unqualified opinion on the U.S. Government's consolidated financial statements. DoD continues to face financial management problems that are pervasive, complex, long-standing, and deeply rooted in virtually all its business operations. DoD's financial management deficiencies adversely affect the Department's ability to control costs and claims on the budget, measure performance, maintain funds control, prevent fraud, and address pressing management issues. GAO first designated this area as high risk in 1995, and it remains so today.

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## Appendix B. Prior Coverage

During the last 5 years, the Government Accountability Office (GAO), the Department of Defense Inspector General (DoD IG), and the Air Force Audit Agency (AFAA) have issued seven reports that discuss the Air Force General Fund, Fund Balance With Treasury account issues and one report that discusses the overall compilation process for an agency Fund Balance With Treasury account. Unrestricted GAO reports can be accessed over the Internet at <http://www.gao.gov>. Unrestricted DoD IG reports can be accessed at <http://www.dodig.osd.mil/audit/reports>. Unrestricted AFAA reports can be accessed at <https://www.afaahq.af.mil/afck/plansreports/reports.shtml>.

### GAO

GAO Report No. GAO-01-847, “Improvements in Air Force Fund Balance With Treasury Reconciliation Process,” July 2001

### DoD IG

DoD IG Report No. D-2005-026, “Reliability of U.S. Army Corps of Engineers, Civil Works, Fund Balance With Treasury and Unexpended Appropriations,” December 28, 2004

DoD IG Report No. D-2005-014, “Independent Auditor’s Report on the Air Force General Funds Fiscal Year 2004 Principal Financial Statements,” November 8, 2004

DoD IG Report No. D-2004-026, “Independent Auditor’s Report on the Air Force General Funds Fiscal Year 2003 Principal Financial Statements,” December 4, 2003

### AFAA

AFAA Report No. F2005-0001-FB3000, “Fund Balance With Treasury for Air Force General and Working Capital Funds,” June 21, 2005

AFAA Report No. F2005-0002-FB2000, “General Accounting and Finance System-Rehost Controls,” March 23, 2005

AFAA Report No. F2005-0001-FB2000, “Statement of Budgetary Resources (General Fund) Financial Data Systems,” February 2, 2005

AFAA Report No. F2003-0004-FB3000, “Air Force General Fund Undistributed Transactions,” November 6, 2002

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## Appendix C. Fund Balance With Treasury

### **Accounting Standards and Criteria for Fund Balance With Treasury.**

Statement of Federal Financial Accounting Standards No. 1, “Accounting for Selected Assets and Liabilities,” March 30, 1993,<sup>\*</sup> defines an agency’s Fund Balance With Treasury as the aggregate amount of funds in the agency’s accounts with Treasury for which the agency is authorized to make expenditures and pay liabilities. Fund Balance With Treasury is an intragovernmental item. From the reporting agency’s perspective, a Fund Balance With Treasury is an asset because it represents the agency’s claim to Federal Government resources. However, from the perspective of the Federal Government as a whole, it is not an asset; and while it represents a commitment to make resources available to Federal departments, agencies, programs, and other entities, it is not a liability.

A Federal entity’s Fund Balance With Treasury includes clearing account balances. An entity’s Fund Balance With Treasury is increased by:

- receiving appropriations, reappropriations, continuing resolutions, appropriation restorations, and allocations received;
- transfers and reimbursements received from other agencies; and
- collections and credits to appropriation or fund accounts that the entity is authorized to spend or use to offset its expenditures.

An entity’s Fund Balance With Treasury is reduced by disbursements made to pay liabilities or to purchase assets, goods and services, investments in U.S. securities, cancellation of expired appropriations, transfers and reimbursements to other entities or to the Treasury, and sequestration or rescission of appropriations.

Agencies should disclose the two parts of the Fund Balance With Treasury balance: the obligated balance not yet disbursed and the unobligated balance. In addition, agencies should explain any discrepancies between Fund Balance With Treasury in their general ledger accounts and the balance in the Treasury’s accounts and explain the causes of the discrepancies in footnotes to the financial statements.

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<sup>\*</sup>The Federal Accounting Standards Advisory Board (the Board) issues Statements of Federal Financial Accounting Standards. In October 1990, the Secretary of the Treasury, the Director of the Office of Management and Budget, and the Comptroller General of the United States established the mission for the Board, to develop accounting standards and principles for the United States Governments. In October 1999, the American Institute of Certified Public Accountants recognized the Board as the organization that promulgates generally accepted accounting principles for Federal entities. In May 2003, the Board added a representative from the Congressional Budget Office to the Board.



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## Appendix D. Glossary

**Allocation.** A delegation, authorized in law, by one agency of its authority to obligate budget authority and outlay funds to another agency.

**Appropriation.** In most cases, appropriations are a form of budget authority provided by law that permits Federal agencies to incur obligations and make payments out of the Treasury for specified purposes. An appropriation usually follows enactment of authorizing legislation. An appropriation act is the most common means of providing budget authority, but in some cases the authorizing legislation itself provides the budget authority.

**Child.** The entity that receives an appropriation/budget authority from another entity account.

**Clearing Account.** Treasury establishes clearing accounts to temporarily hold unidentified general, special, or trust collections that subsequently will be credited to the proper receipt or expenditure account of the Federal entity. Clearing accounts are preceded by an “F” followed by a fund account symbol in the “3800” series group.

**Defense Departmental Reporting System – Audited Financial Statements (DDRS-AFS).** DDRS-AFS is a DoD application that facilitates the preparation and audit of DoD financial statements, and required supplementary information.

**Defense Departmental Reporting System-Budgetary (DDRS-B).** DDRS-B is designed to standardize the DoD departmental reporting process and produce the monthly departmental budgetary reports based on the United States Standard General Ledger and standard attributes.

**Deposit Fund.** Treasury establishes a deposit fund account to record monies that do not belong to the Federal Government.

**FMS (Financial Management Service) 6200 “Appropriation Warrant” (Hard-copy Appropriation Warrants).** A hard-copy appropriation warrant is a financial control document, issued pursuant to law (usually appropriation acts) by Treasury, that establishes the amount of monies authorized to be withdrawn (disbursed) from the central accounts that are maintained by Treasury. The hard-copy appropriation warrant is the basis for recording appropriations (cash) on the books of Treasury and the DoD.

**General Accounting and Finance System-Rehost (GAFS-R).** GAFS-R is the official DFAS Denver department accounting system. GAFS-R was implemented in FY 2004. DFAS Denver uses GAFS-R to prepare financial statements and reports.

**General Fund.** Treasury establishes general fund expenditure accounts to record amounts appropriated by Congress for the general support of the Government.

**Government On-Line Accounting Link Information Access System II (GOALS II).** This is the system that allows Treasury to receive agency accounting data and distribute agency accounting reports. The system includes

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many different subsystems for different financial accounting and reporting purposes.

**Invisible Warrants.** Treasury transfers the funds from available receipt accounts to expenditure accounts through invisible warrants.

**Parent.** This is the entity that transfers an appropriation/budget authority to another entity account.

**Revolving Fund.** Revolving funds are authorized by specific provisions of law to finance a continuing cycle of business-type operations. The receipts are credited directly to the revolving fund as offsetting collections and are available for expenditure without further action by Congress.

**Special Fund.** Treasury establishes special fund expenditure accounts to record amounts appropriated from special fund receipts. Agencies may expend those receipts for special programs according to specific provisions of law.

**SF (Standard Form) 1219, “Statement of Accountability.”** Each DoD disbursing station is required to prepare the Statement of Accountability monthly. The Statement of Accountability reports information to the Treasury on deposits, interagency transfers, and checks issued. The Statement of Accountability also reports net disbursements—the sum of the deposits, interagency transfers, and checks issued that month.

**SF 1220, “Statement of Transactions.”** Each DoD disbursing station is required to prepare the Statement of Transactions monthly. The Statement of Transactions reports the disbursements shown on the Statement of Accountability by appropriation. Treasury requires that the net disbursements reported on the Statement of Transactions agree with the net disbursements reported on the Statement of Accountability.

**Transfer.** To reduce budgetary resources (budget authority and unobligated balances) in one account and increase them in another, by the same amount.

**Trust Fund.** Treasury establishes trust fund expenditure accounts to record amounts appropriated from trust fund receipts. Agencies may expend those receipts for specific purposes or programs according to the terms of a trust agreement or statute.

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## Appendix E. Treasury Fund Symbols and Expenditure and Receipt Accounts

Treasury and OMB assign, amend, change, and discontinue account symbols and titles. The account symbols represent individual appropriations, receipts, and other fund accounts by agency. The account symbols are used to report to Treasury and OMB. Treasury provides a listing of all assigned symbols and titles in the *Federal Account Symbols and Titles Book*.

Expenditure and receipt accounts are classified by Treasury and then assigned to a fund group based on their characteristics and the nature of the transactions they support. Treasury and OMB classify transactions within fund groups by assigning numeric or alphanumeric account symbols. After considering the Government's relationship to the accounts, the availability of the funds for expenditure, and the sources of the receipts; Treasury assigns the account symbols to agencies.

**Expenditure Accounts.** Treasury uses the following fund groups for expenditures:

- General fund expenditure accounts are created by Treasury to record amounts appropriated by Congress for the general support of the Government.
- Management fund accounts are created by Treasury to facilitate accounting for administration of intragovernmental activities other than a continuing cycle of operations. These accounts are working fund accounts that are authorized by law.
- Revolving fund accounts are created by Treasury to record funds authorized by specific provisions of law to finance a continuing cycle of business-type operations. Receipts are credited as offsetting collections directly to the revolving fund. They are then available for expenditure without any further action by Congress. The receipts are classified by Treasury as public enterprise funds, in which receipts come primarily from sources outside the Government, or intergovernmental funds, in which receipts come primarily from other appropriations or funds.
- Special fund expenditure accounts are created by Treasury to record amounts appropriated from special fund receipts. These receipts may be used by agencies for special programs according to specific provisions of law.
- Deposit fund accounts are created by Treasury to record monies that do not belong to the Federal Government.
- Trust fund expenditure accounts are created by Treasury to record amounts appropriated from trust fund receipts. These receipts may be used by agencies for specific purposes or programs according to the terms of a trust agreement or statute. Trust revolving funds are created by Treasury when a law authorizes a revolving fund and designates the

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revolving fund as a trust fund. In all other regards, they are the same as a revolving fund.

Expenditure account symbols consist of seven or more digits. The first 2 digits identify the agency responsible for the account. The next digits represent the period of availability for the obligation. The last four digits identify the specific account by fund group.

Table E-1 shows how Treasury classifies expenditure accounts and assigns symbols by fund groups and major classes.

<b>Table E-1. Classification of Expenditure Accounts by Treasury</b>	
<u>Fund Group</u>	<u>Major Class</u>
General fund accounts	0000-3799
Clearing accounts	3800-3899
Management fund	3960-3999
Revolving fund	4000-4999
Public enterprise	4000-4499
Intragovernmental	4500-4999
Special fund	5000-5999
Deposit fund	6000-6999
Trust fund	8000-8399 and 8500-8999
Trust revolving fund	8400-8499

The period of availability is identified by the account symbol as follows:

- Annual appropriations are designated with a single digit that indicates the fiscal year of availability for incurring obligations of a 1-year appropriation.
- Multiple-year appropriations are designated with two digits separated by a slash for incurring obligations for a definite period in excess of one fiscal year. The digit preceding the slash indicates the first fiscal year of availability, and the digit immediately following the slash indicates the final fiscal year of availability.
- No-year appropriations are designated with an “X” to indicate that the appropriation is available for obligations for an indefinite period of time.

For example, the account symbol for the Air Force operation and maintenance appropriation for FY 2005 would be 57 05 3400.

In addition, transfer appropriation accounts are created by Treasury to receive, and later obligate and disburse, allocations treated as nonexpenditure transactions. These accounts are symbolized by adding the receiving agency’s department prefix to the original appropriation or fund account symbol.

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For example, the account symbol for the Air Force transfer of FY 2005 operation and maintenance funds to the Department of Transportation would be 69 57 05 3400.

**Receipt Accounts.** Treasury uses the following fund groups for receipts:

- General fund receipt accounts are credited by Treasury with all receipts not earmarked by law for a specific purpose.
- Special fund receipt accounts are credited by Treasury with receipts from specific sources earmarked by law for specific purposes. Depending on statutory requirements, after collection, these receipts may be available immediately or unavailable for expenditures.
- Trust fund receipt accounts are credited by Treasury with receipts generated by a trust agreement or statute that designates a fund as a trust fund. Depending on statutory requirements, after collection, these receipts may be available immediately or unavailable for expenditures.
- Clearing accounts are created by Treasury to temporarily hold unidentifiable general, special, or trust funds collections that belong to the Government until they are classified to the correct receipt or expenditure account by the Government agency. The accounts can be identified by the “F” preceding the last four digits of the fund account symbol.

Receipt account symbols usually consist of six digits with the exception of receipt clearing accounts and available receipt accounts. The first two digits identify the agency which is administratively responsible for the receipts. The last four digits (Major Class) identify the account within that fund group.

Table E-2 shows how Treasury classifies receipt accounts and assigns symbols by fund groups and major classes.

<b>Table E-2. Classification of Receipt Accounts by Treasury</b>	
<u>Fund Group</u>	<u>Major Class</u>
General fund accounts	0100-3000
Clearing accounts	3800
Special fund receipt accounts	5000-5999
Trust fund receipt accounts	8000-8999

Available receipts are special or trust fund receipts that, pursuant to law, are available as appropriations to a single agency for expenditure without further congressional action. An available receipt account uses the same symbol as its corresponding expenditure account except that an “X” is inserted to specify the period of availability of such funds for obligation. Unavailable receipts are receipts that, when collected, are not appropriated and not immediately available

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for expenditure. The funds are unavailable either because Congress limited the amount available for expenditure or agencies cleared amounts credited to receipt accounts, in whole or in part, to other receipt accounts before taking appropriation warrant action.

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## Appendix F. Treasury Reports for Fund Balance With Treasury

Treasury prepares five Fund Balance With Treasury reports including three Fund Balance With Treasury reports for receipt accounts and two Fund Balance With Treasury reports for expenditure accounts.

**Treasury Reports for Receipt Accounts.** The three Fund Balance With Treasury reports for receipt accounts are the:

- FMS 6655, “Receipt Account Trial Balance,”<sup>1</sup>
- FMS 6655, “Receipt Account Ledger,”<sup>2</sup> and
- FMS 6655, “Report of Unavailable Receipt Transactions.”<sup>3</sup>

The three reports include summary information for each receipt account regarding:

- current month receipts and
- fiscal year-to-date Fund Balance With Treasury.

**Treasury Reports for Expenditure Accounts.** The two Fund Balance With Treasury reports for expenditure accounts are the:

- FMS 6654, “Undisbursed Appropriation Account Trial Balance,”<sup>4</sup> and
- FMS 6653, “Undisbursed Appropriation Account Ledger.”<sup>5</sup>

The two reports show the same summary information for each expenditure account:

- beginning fiscal year Fund Balance With Treasury,
- fiscal year-to-date appropriations,
- fiscal year-to-date nonexpenditure transfers,

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<sup>1</sup>The FMS 6655, “Receipt Account Trial Balance,” reports both available and unavailable receipt accounts. Treasury issues the FMS 6655, “Receipt Account Trial Balance,” every month for each applicable account (including accounts with no transactions during the month).

<sup>2</sup>Treasury issues the FMS 6655, “Receipt Account Ledger,” for accounts with transactions during the month but does not list accounts that had no transactions during the month.

<sup>3</sup>The FMS 6655, “Report of Unavailable Receipt Transactions,” reports only unavailable receipt accounts. Treasury issues this report for accounts with transactions during the month but does not list accounts that had no transactions during the month.

<sup>4</sup>Treasury issues the FMS 6654, “Undisbursed Appropriation Account Trial Balance,” every month for each applicable account (including accounts with no transactions during the month).

<sup>5</sup>Treasury issues the FMS 6653, “Undisbursed Appropriation Account Ledger,” for accounts with transactions during the month but does not list accounts that had no transactions during the month.

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- fiscal year-to-date net disbursements,<sup>6</sup> and
  - fiscal year-to-date Fund Balance With Treasury.

The fiscal year-to-date appropriations line includes appropriation warrants issued by Treasury on the FMS 6200, “Department of the Treasury Appropriation Warrant,” or in invisible form.<sup>7</sup>

The fiscal year-to-date nonexpenditure transfers line includes nonexpenditure transfers made by Treasury on the SF 1151, “Nonexpenditure Transfer Authorization.”

The fiscal year-to-date net disbursements line includes net disbursements that agencies report to Treasury, by account, on statements of transactions.<sup>8</sup>

Therefore, the three lines provide the universe by transaction type (appropriation warrants, nonexpenditure transfers, and net disbursements) applicable to each expenditure account.

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<sup>6</sup>The reports also show the net disbursements by agency location code (ALC). The first two numbers of the agency location code represent the agency to which the Treasury has assigned the disbursing station. For example, net disbursements with an agency location code beginning with Treasury Index 21 represent disbursing stations that the Treasury assigned to the Army. Army disbursing stations now report to the Defense Finance and Accounting Service (DFAS) Indianapolis.

<sup>7</sup>Treasury does not issue an FMS 6200, “Department of the Treasury Appropriation Warrant,” for certain funds reported as fiscal year-to-date appropriations. Funding provided without issuance of a FMS 6200, “Department of the Treasury Appropriation Warrant,” is referred to as an invisible warrant.

<sup>8</sup>Agencies with disbursing authority report net disbursements by account on statements of transactions. DoD agencies use the SF 1220, “Statement of Transactions,” and the DD 1329, “Statement of Transactions.” The Department of State reports net disbursements by account on the SF 1221, “Statement of Transactions (Foreign Service Accounts).”



## Appendix G. List of Expenditure and Receipt Accounts Not Reconciled from the GAFS-R Trial Balance

Table G-1 lists the 91 expenditure accounts reported by Treasury for the General Fund on the September 30, 2004, FMS 6654 "Undisbursed Appropriation Account Trial Balance" that were not reconciled from the General Fund September 30, 2004, GAFS-R trial balance for the FBWT 1010 account.

<b>Table G-1. Expenditure Accounts Not Reconciled</b>				
	<u>With Activity</u>	<u>Never Had Activity</u>	<u>FY 2004 Activity</u>	<u>FY 2004 Ending Balance</u>
57 02 0704	X			
57 0206 0704	X			
57 0509 0740		X		
57 05 0745		X		
57 X 1997	X			
57 X 1998	X			
57 M 3010	X			
57 01 3010	X			
57 02 3010	X			
57 0102 3010		X		
57 03 3010		X		
57 0203 3010	X			
57 0104 3010		X		
57 0304 3010		X		
57 0205 3010		X		
57 0306 3010		X		
57 0507 3010		X		
57 0001 3011		X		
57 0102 3011		X		
57 0203 3011		X		
57 0304 3011		X		
57 0507 3011		X		
57 00 3012	X			
57 01 3012		X		
57 02 3012		X		
57 03 3012		X		
57 X 3013	X			
57 M 3020	X			
57 0507 3020		X		
57 M 3080	X			
57 99 3080	X			
57 0104 3080		X		
57 0205 3080		X		
57 0306 3080		X		
57 0507 3080		X		

<b>Table G-1. Expenditure Accounts Not Reconciled (cont'd)</b>				
	<u>With Activity</u>	<u>Never Had Activity</u>	<u>FY 2004 Activity</u>	<u>FY 2004 Ending Balance</u>
57 M 3300	X			
57 00 3300	X		X	
57 01 3300	X			
57 02 3300	X			
57 03 3300	X			
57 0306 3300		X		
57 0509 3300		X		
57 M 3400	X			
57 0102 3400	X			
57 0304 3400		X		
57 05 3400		X		
57 M 3500	X			
57 0102 3500	X			
57 0203 3500		X		
57 0304 3500		X		
57 05 3500		X		
57 M 3600	X			
57 02 3600	X			
57 03 3600	X			
57 0506 3600		X		
57 M 3700	X			
57 05 3700		X		
57 0509 3730		X		
57 M 3740	X			
57 0102 3740		X		
57 0203 3740		X		
57 0304 3740		X		
57 05 3740		X		
57 00 3830		X		
57 01 3830		X		
57 02 3830		X		
57 03 3830		X		
57 0509 3830		X		
57 M 3840	X			
57 0102 3840		X		
57 0203 3840		X		
57 0304 3840		X		
57 05 3840		X		
57 M 3850	X			
57 05 3850		X		
57 11 0203 1081		X		
57 11 0304 1081		X		
57 11 05 1081		X		
57 11 05 1082		X		
57 X 6002	X			
57 X 6031	X			

<b>Table G-1. Expenditure Accounts Not Reconciled (cont'd)</b>				
	<u>With Activity</u>	<u>Never Had Activity</u>	<u>FY 2004 Activity</u>	<u>FY 2004 Ending Balance</u>
57 00 6060		X		
57 01 6060		X		
57 02 6060		X		
57 X 6113	X			
57 99 6763	X			
57 05 6763		X		
57 F 0152	X			X
57 F 3875 001	X		X	
57 F 3885 007	X		X	
57 F 3886	X			

Table G-2 lists the 22 receipt accounts reported by Treasury for the General Fund on the September 30, 2004, FMS 6655 "Receipt Account Trial Balance" that were not reconciled from the General Fund September 30, 2004, GAFS-R trial balance for the FBWT 1010 account.

<b>Table G-2. Receipt Accounts Not Reconciled</b>			
	<u>With Activity</u>	<u>FY 2004 Activity</u>	<u>FY 2004 Ending Balance</u>
57 0869	X		
57 0891	X		
57 1030	X		
57 1060	X	X	X
57 1099	X	X	X
57 1125	X		
57 1210	X	X	X
57 1299	X	X	X
57 1435	X	X	X
57 2462	X		
57 2621	X		
57 2641	X		
57 3102 001	X		
57 3102 002	X		
57 3102 003	X		
57 3200	X	X	X
57 3220	X		
57 5095 001	X	X	X
57 8928 001	X	X	X
57 8928 002	X	X	X
57 8928 021	X		
57 8930 002	X		

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## Appendix H. Checklists for Reviewing Financial Management Systems

**GAO Checklist.** GAO-05-225G, “Checklist for Reviewing Systems under the Federal Financial Management Improvement Act,” February 2005, states, “There is no requirement that this checklist be used in assessing core financial systems. Rather, it is provided as a tool for use by experienced staff and is one in a series of documents we have issued to assist agencies in improving or maintaining effective operations.” The GAO Checklist also states, “The Federal Financial Management Improvement Act of 1996 (FFMIA) requires, among other things, that agencies implement and maintain financial management systems that substantially comply with federal financial management system requirements.” In addition, the GAO Checklist states,

OMB’s 2001 implementation guidance provides the agency heads and inspectors general with a means for determining whether their agencies’ financial management systems substantially comply with federal financial management system requirements. Agencies can use this checklist as a tool to help determine compliance with federal financial management system requirements as well as to assist in their annual reporting on such compliance as required by 31 U.S.C. § 3512(d).

The GAO Checklist further states “Completing this checklist will allow agencies to systematically determine whether specific systems requirements are being met. In determining compliance with FFMIA requirements, agencies should assess the results of the completed checklist based on the core financial system requirements taken as a whole.” Additionally, the GAO Checklist states,

Functional requirements have been established to provide the basic information and control needed to carry out financial management functions; manage the financial operations of an agency; and report on the agency’s financial status to central agencies, Congress, and the public. This includes data needed to prepare the principal financial statements for federal agencies in accordance with OMB Bulletin No. 01-09, Form and Content of Agency Financial Statements.

**DFAS Blue Book.** DFAS 7900.4G, “A Guide to Federal Requirements for Financial Management Systems,” (Blue Book ), Version 4.1.2, November 2004, states,

While this document represents an extensive compilation of Federal requirements applicable to DoD’s financial management systems, it does not necessarily include all requirements that pertain to such systems. A myriad of requirements applicable to Federal financial management systems exists in dozens of different authoritative sources. This document contains hundreds of requirements promulgated by the central agencies and DoD. As such, the document represents a valuable tool for systems managers, operators, programmers, and accountants to use in planning, developing, implementing, modifying, and evaluating financial management systems. The intent of this document, as a tool, is to focus management’s attention on the

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requirements financial management systems must satisfy. Management, however, is explicitly responsible for being knowledgeable of the actual laws and regulations and ensuring that their systems comply with them.

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## Appendix I. Hierarchy of Accounting Standards

The American Institute of Certified Public Accountants designated the Federal Accounting Standards Advisory Board (FASAB) as the body that establishes accounting principles for Federal entities. The American Institute of Certified Public Accountants hierarchy of generally accepted accounting principles (GAAP) in Statement of Auditing Standards No. 91, “The Federal GAAP Hierarchy,” governs what constitutes GAAP for U.S. Government reporting entities. The hierarchy lists the priority sequence of sources that an entity should look to for accounting and reporting guidance.

For financial statements of Federal Government entities, the GAAP hierarchy is:

- FASAB Statements and Interpretations.
- FASAB Technical Bulletins.
- FASAB Accounting and Auditing Committee Technical Releases and the AICPA Accounting Standards Executive Committee Practice Bulletins.
- FASAB implementation guides and common business practices within the Federal Government.

Further, the DoD FMR, Volume 1, Chapter 8, “Hierarchy of Accounting Standards,” May 1998, sets forth the accounting standards that shall be followed by DoD. Chapter 8 states that the following criteria comprise Federal GAAP and must be followed by DoD and each DoD Component:

- SFFASs,
- Interpretations related to SFFASs,
- OMB’s Form and Content Bulletin,
- Accounting Principles published by other authoritative standard-setting bodies and authoritative sources if the use of such accounting principles improves the meaningfulness of the financial statements,
- U.S. Government Standard General Ledger
- Policies and guidance published in the DoD FMR, and
- Interim policies and guidance issued by the OUSD(C)/CFO through various memoranda.

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## Appendix J. Elements of a Management Control Program

DoD Instruction 5010.40, “Management Control (MC) Program Procedures,” August 28, 1996, requires DoD Components to develop a MC Program that includes the following elements:

- **Establish a Management Control Process.** Each DoD Component should establish a MC process that will conclude with the reporting of management’s opinion about the effectiveness of its MCs. This process must include, as appropriate, assigning responsibilities and providing personnel for planning, directing, and executing the MC Program; developing internal reporting and tracking capabilities; ensuring periodic evaluations of MCs; and maintaining appropriate documentation.
- **Segment into Assessable Units.** Each DoD Component should establish and maintain an inventory of its assessable units segmented along organizational, functional, or programmatic lines.
- **Evaluate the Effectiveness of Management Controls.** Each DoD Component should establish an evaluation process or mechanism to meet its specific requirements.
- **Identify, Report, and Correct Material Weaknesses.** Each DoD Component should establish and maintain a process that identifies, reports, and corrects MC weaknesses.
- **Establish Senior Management Council.** Each DoD Component should establish a senior management council to assess and monitor MC Program efforts.
- **Submit an Annual Statement of Assurance.** Each DoD Component should submit an annual statement of assurance based on a general assessment of the effectiveness of the MCs.

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## **Appendix K. Report Distribution**

### **Office of the Secretary of Defense**

Under Secretary of Defense (Comptroller)/Chief Financial Officer  
Deputy Chief Financial Officer  
Deputy Comptroller (Program/Budget)  
Director, Program Analysis and Evaluation

### **Department of the Army**

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

### **Department of the Navy**

Naval Inspector General  
Auditor General, Department of the Navy  
President, Naval Postgraduate School

### **Department of the Air Force**

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

### **Combatant Command**

Inspector General, U.S. Joint Forces Command

### **Other Defense Organizations**

Director, Defense Contract Audit Agency  
Director, Defense Contract Management Agency  
Director, Defense Finance and Accounting Service  
Director, Defense Intelligence Agency  
Director, Defense Logistics Agency  
Director, National Security Agency  
President, Defense Systems Management College

### **Non-Defense Federal Organization**

Office of Management and Budget



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## **Congressional Committees and Subcommittees, Chairman and Ranking Minority Member**

Senate Committee on Appropriations  
Senate Subcommittee on Defense, Committee on Appropriations  
Senate Committee on Armed Services  
Senate Committee on Homeland Security and Governmental Affairs  
House Committee on Appropriations  
House Subcommittee on Defense, Committee on Appropriations  
House Committee on Armed Services  
House Committee on Government Reform  
House Subcommittee on Government Efficiency and Financial Management, Committee on Government Reform  
House Subcommittee on National Security, Emerging Threats, and International Relations, Committee on Government Reform  
House Subcommittee on Technology, Information Policy, Intergovernmental Relations, and the Census, Committee on Government Reform



# Office of the Under Secretary of Defense Comments



COMPTROLLER

OFFICE OF THE UNDER SECRETARY OF DEFENSE  
1100 DEFENSE PENTAGON  
WASHINGTON, DC 20301-1100

NOV 17 2005

MEMORANDUM FOR PROGRAM DIRECTOR, FINANCIAL RESOURCES  
DIVISION, OFFICE OF INSPECTOR GENERAL,  
DEPARTMENT OF DEFENSE

SUBJECT: Draft Report Entitled "Report on Internal Controls Over the Compilation  
of the Air Force, General Fund, Fund Balance with Treasury for FY 2004"  
(Project No. D2005FP-D000FP-0074)

This is in response to the subject draft report of October 21, 2005, provided to this  
office for review and comments. We appreciate the opportunity to review the draft and  
provide comments.

We agree with the recommendations to improve guidance for accounting and  
reporting Fund Balance with Treasury (FBWT). My office will update the DoD  
Financial Management Regulation and our website, as appropriate. We concur with the  
recommendation that my office work with the Office of Management and Budget (OMB)  
and Department of Treasury to propose revised accounting treatment for allocation  
transfers. Based on our interpretation of OMB Circular A-136, we do not concur with the  
recommendation that clearing accounts be considered nonentity accounts.

In addition, we believe that receipt accounts should be included as part of FBWT  
per guidance in the Treasury Financial Manual Volume 1, Part 2, Chapter 5100, Section  
5130. More detailed comments are in the attachment.

My point of contact for this matter is Ms. Maryla Engelking. She may be reached  
by e-mail at [maryla.engelking@osd.mil](mailto:maryla.engelking@osd.mil) or by telephone at (703) 697-3192.

A handwritten signature in black ink, reading "Teresa McKay".

Teresa McKay  
Deputy Chief Financial Officer

Attachment:  
As stated

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**DoD OIG DRAFT REPORT DATED OCTOBER 21, 2005**  
**DoD OIG D2005FP-D000FP-0074**

**REPORT ON INTERNAL CONTROLS OVER THE COMPILATION OF THE  
AIR FORCE, GENERAL FUND, FUND BALANCE WITH TREASURY FOR  
FISCAL YEAR 2004**

**RECOMMENDATIONS A.1.a, A.1.b, A.1.c, A.1.d, A.1.e and A.1.f:** The Department of Defense (DoD) Office of Inspector General (OIG) recommends that the Office of Under Secretary of Defense, Comptroller (OUSD(C)) revise DoD Regulation 7000.14-R, Financial Management Regulation (FMR) Volume 4, Chapter 2, "Accounting for Cash and Fund Balance with Treasury" to establish specific procedures for the reconciliation of Fund Balance with Treasury (FBWT) and the periodic review of the validity of all expenditure and receipt accounts being reported by the Department of Treasury.

**DoD RESPONSE:** Concur with comment. The FMR will be revised to state that United States Standard General Ledger account 1010, Fund Balance with Treasury, must be reconciled with the applicable Department of Treasury reports or the Account Summary Report in the Department of Treasury Government-Wide Accounting System. The FMR will state the frequency and timeliness of the reconciliation. It will also require an annual validation by DFAS of the DoD accounts being reported in the applicable Treasury reports or the Account Summary. The FMR will not list the specific procedures, but will direct the reader to the Department of Treasury FBWT reconciliation procedures.

**RECOMMENDATIONS B.1.a, B.1.b, B.1.d, and B.1.e:** The DoD OIG recommends that OUSD(C) provide guidance for classifying expenditure accounts as entity or nonentity and fund type by revising the FMR Volume 6B, Chapter 10, and Appendix A.

**DoD RESPONSE:** Concur with comment. Appendix A to Volume 6B will be deleted. Information that is presented in this Appendix is included in quarterly financial statement guidance posted on the OUSD(C) website and also on the Defense Finance and Accounting Services (DFAS) e-portal. The information to be posted on the website and e-portal includes appropriations and fund symbols by reporting entity. Volume 6B, Chapter 10, will refer the reader to the OUSD(C) website.

**RECOMMENDATION B.1.c:** The DoD OIG recommends that clearing accounts be classified as nonentity accounts according to Office of Management and Budget (OMB) Bulletin 01-09.

**DoD RESPONSE:** Nonconcur. OMB Circular A-136 and Bulletin 01-09 both state, "To the extent that the reporting entity maintains fund balance in deposit, suspense, and

Attachment  
Page 1 of 3

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clearing accounts that are not available to finance the entity's activities, those balances should be disclosed as nonentity assets." DoD contends that the funds currently in DoD's clearing accounts are available to finance the entity's activities; therefore, they are entity accounts.

**DoD COMMENT:** In the discussion relating to Recommendation B, DoD OIG states that receipt accounts should not be included as part of FBWT. Treasury Financial Manual Volume 1, Part 2, Chapter 5100, Section 5130 states, "Agencies must post all transactions that affect FBWT and are reported on their SOTs (Statement of Transactions) to a corresponding SGL 1010 account in their internal general ledger. Agencies must reconcile the SGL 1010 account balances for each fund symbol with Treasury's records (FMS 6653 and 6655) monthly." Receipt accounts are reported on the FMS 6655; therefore, they must be included in FBWT as nonentity.

**RECOMMENDATION C.1.a:** The DoD OIG recommends that FMR Volume 6A, Chapter 2, be revised to require the disclosure of applicable criteria to support the rationale for journal voucher adjustments on the journal voucher or supporting documentation.

**DoD RESPONSE:** Concur. Quarterly financial statement guidance on the OUSD(C) website contains this requirement. It will also be added to the FMR.

**RECOMMENDATION C.1.b:** The DoD OIG recommends that FMR Volume 6A, Chapter 2, be revised to require the disclosure of specific expenditure or receipt accounts affected by the journal voucher.

**DoD RESPONSE:** Concur. The FMR will be revised to state that specific expenditure or receipts must be included in the support documentation at the time the FBWT journal voucher is created.

**RECOMMENDATION C.1.c:** The DoD OIG recommends that FMR Volume 6A, Chapter 2, be revised to require the disclosure of the calculation of the dollar amount of the adjustment.

**DoD RESPONSE:** Concur. The FMR will be revised to include this disclosure within the journal voucher description or where this information can be found.

**RECOMMENDATIONS D.1.a and D.1.b:** The DoD OIG recommends that OUSD(C) coordinate with OMB to revise OMB Circular A-11, "Preparation, Submission, and Execution of the Budget," and with the Department of Treasury to revise Treasury Financial Manual Volume 1, Part 2, Chapter 4700, "Agency Reporting Requirements for

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the Financial Report of the U.S. Government,” to require the recipient of the transfer to report the financial activity on their financial statements.

**DoD RESPONSE:** Concur. The Form and Content Subcommittee of CFO Council has formed a workgroup whose goal is to investigate and propose revised accounting treatment for allocation transfers. This workgroup is chaired by a member of the OUSD(C) staff.

**RECOMMENDATION D.1.c:** The DoD OIG recommends that FMR Volume 6B, Chapter 10, be revised to establish and incorporate a policy for identifying the expenditure and receipt accounts used in the calculation of Line 2.A. “Fund Balance per Treasury” of Note 3, “Fund Balance with Treasury.”

**DoD RESPONSE:** Concur with comment. Due to the changeable list of expenditure and receipt accounts, this information will be included in quarterly guidance posted on the OUSD(C) website and also on the DFAS e-portal. The FMR will refer the reader to the OUSD(C) website.

# Defense Finance and Accounting Service Comments



DEFENSE FINANCE AND ACCOUNTING SERVICE  
ARLINGTON  
1851 SOUTH BELL STREET  
ARLINGTON, VA 22240-5291

SEP 12 2005

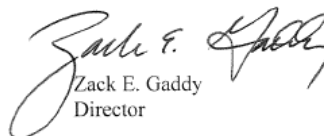
MEMORANDUM FOR TECHNICAL DIRECTOR, AUDIT FOLLOWUP & GAO AFFAIRS,  
OFFICE OF THE INSPECTOR GENERAL, DEPARTMENT OF  
DEFENSE

SUBJECT: "Internal Controls Over the Compilation of the Air Force, General Fund, Fund  
Balance With Treasury for FY 2004," (DoDIG Project No. D2005FP-0074),  
dated August 12, 2005

Overall, we non-concur with the final conclusions as documented in the subject draft report. Specifically, we do not agree that DFAS Denver's internal controls over the General Fund's Fund Balance With Treasury accounts were inadequate resulting in the September 30, 2004, General Fund financial statements being unfairly represented. We had previously discussed each finding with the DoDIG audit team based on their Discussion Draft report. As little was changed from the discussion draft to the resulting draft audit report, our position remains that none of the audit findings were proven to identify any material or substantive deficiencies. We do not, for the most part, take exception to the improvements recommended in the audit report. However, we non-concur with the adverse affect the report attempts to portray resulting from the specific findings identified. This is particularly true considering the dollar impacts mentioned in the audit which were never proven to have impacted the financial statement line item data as reported.

The audit report's findings and recommendations were directed at both DFAS Denver and OUSD(C)/CFO. Therefore, with regard to the report's recommendations, we provided specific comments to recommendations that were directed at DFAS Denver - A.2, B.2, C.2, D.2, and E.1.

Questions your staff may have concerning the audit may be directed to Mr. Dan Valdez, DFAS-ADN/DE, (303) 676-7253 or DSN 926-7253.

  
Zack E. Gaddy  
Director

Attachment:  
As stated

[www.dod.mil/dfas](http://www.dod.mil/dfas)  
Your Financial Partner @ Work

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**OIG Draft Report “Internal Controls Over the Compilation of the Air Force, General Fund, Fund Balance With Treasury for FY 2004,”  
(DoD Project No. D2005FP-0074), dated August 12, 2005**

Summary of Management Responses to Recommendations were as follows:

Recommendation(s) A.2.a.(1), A.2.a.(2) – Concur (Not Material)  
A.2.b., A.2.c.(1)-(6) – Concur (Not Material)

Recommendation(s) B.2.a. – Concur (Not Material)  
B.2.b.(1)-(6) – Non-concur

Recommendation(s) C.2. a., b., c. – Concur (Not Material)

Recommendation(s) D.2 – Concur (Not Material)

Recommendation(s) E.1 – Non-concur

**Recommendation A.2.** We recommend that the Director of Defense Finance and Accounting Service Denver:

- a. Determine whether the 113 expenditure and receipt accounts not reconciled are valid and are still being used by the Air Force General Fund.
  - (1) If an account is valid and still being used by the Air Force General Fund, establish the expenditure or receipt account in the General Accounting and Finance System-Rehost.
  - (2) If an account is invalid and not being used by the Air Force General Fund, coordinate with Treasury to have the expenditure or receipt account removed from Treasury reports.
- b. Delete Operating Instruction 17, “Fund Balance With Treasury: Reconciliation Between Departmental Reporting Centers and Treasury Disbursements and Collections,” November 1, 2003.
- c. Establish formal standard operating procedures to implement the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer requirements for reconciling expenditure and receipt accounts by establishing procedures for:
  - (1) Identifying the specific Treasury reports that Defense Finance and Accounting Service Denver should use to reconcile their expenditure and receipt accounts on a monthly basis.
  - (2) Requiring Defense Finance and Accounting Service Denver to review all the expenditure and receipt accounts reported on Treasury reports to determine



whether they are valid accounts and are still being used for the Air Force General Fund.

- (3) Requiring Defense Finance and Accounting Service Denver to establish valid accounts and accounts that are still being used by the Air Force General Fund in the Defense Finance and Accounting Service Denver General Accounting and Finance System-Rehost.
- (4) Requiring Defense Finance and Accounting Service Denver to coordinate with Treasury to remove from Treasury accounts the invalid accounts or accounts that are not being used by the Air Force General Fund.
- (5) Establishing time periods for reconciling expenditure and receipt accounts and reporting the results of the reconciliation, based on policy established by the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer.
- (6) Requiring the appropriate signature on the standard operating procedures and making these procedures part of the Defense Finance and Accounting Service standard operating procedures.

**Management Comments. A.2.a.(1) & A.2.a.(2).** Concur. The 113 expenditure and receipt accounts identified were validated to determine any impact on the financial statement reporting baseline. None were found to have a material affect on the FY 2004 financial statement data as reported. However, corrective actions taken and our review results are as follows:

DFAS-DE reconciles general ledger account (GLA) 1010 in GAFS-R accounting records to amounts on Treasury reports, on a monthly basis and submits this reconciliation monthly to OUSD (C). Audit finding suggests that expenditures and receipt accounts with ending balances for FY 2004 of zero were not reconciled just because these zero balance accounts were not on the spreadsheet. This is not the case.

- 103 of the 113 accounts cited in Appendix G, had zero ending balances. Most of these were invalid appropriations created by Treasury as part of their account rollover process but never used. Twelve of the 103 represent FY 05 accounts cloned by Treasury prematurely and reflected at September 2004 on Treasury reports. Treasury removed 70 of the 103 invalid accounts with zero balances in July 2005 as requested by DFAS-DE.
- 9 of the 113 accounts were receipt accounts. Total receipt accounts of \$151,974,093.78 were included in Line 2A. Fund Balance per Treasury. In accordance with Treasury's Notice of Correction to USSGL Section III, TFM Transmittal Letter S2-04-02, dated September 2004, we preclosed from the Air Force receipt account balance \$151,054,048.45 in miscellaneous receipts. The resulting reconciliation difference due to preclosing of agency miscellaneous receipt accounts, as required by guidance, was included in the reconciling amount as noted in the narrative in Note 3A, Fund Balance with Treasury. DFAS-DE did not preclose the difference of \$920,045.33 because at the

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time we did not consider receipt account 5095 as a miscellaneous receipt account. This amount is reflected in both agency FBWT and Treasury and not a part of the reconciling amount. Therefore, there was no material impact on the financial statement data as reported.

- 1 of the 113 accounts was a budget clearing account that was included on the financial statement under a pseudo account.

Additionally, DFAS-DE has taken corrective action to establish receipt accounts in GAFS-R. This will facilitate the inclusion of receipt accounts in our monthly reconciliation. Also, valid expenditure and suspense accounts with zero balances will now be included on monthly reconciliations.

**Estimated Completion Date.** November 30, 2005 (Applies to A.2.a.(1) & A.2.a.(2.)

Point of Contact. Sylvia Taylor-Porter/ADGG/303-676-7750

**Management Comments. A.2.b., A.2.c. (1) – (6).** Concur. However, this finding did not disclose any material deficiency as a result of lack of operating instructions causing errors in balances reported, invalid zero balance accounts on the Treasury Trial Balance, or receipt accounts not included in GAFS-R. As per the recommendation, Operating Instruction 17 has been rescinded. Standard operating procedures are being formalized and updated in accordance with revised DoD Regulation 7000.14-R, Volume 4, Chapter 2 as recommended in A.1, and/or other interim guidance provided by OUSD (C).

**Estimated Completion Date.** December 31, 2005 (Applies to A.2. b., & c.)

Point of Contact. Sylvia Taylor-Porter/ADGG/303-676-7750

**Recommendation B.2.** We recommend that the Director of Defense Finance and Accounting Service Denver modify the General Accounting and Finance System-Rehost to properly capture and categorize expenditure accounts as:

- a. Entity or non-entity.
- b. The following fund types:
  - (1) General Fund
  - (2) Deposit Fund
  - (3) Trust Fund
  - (4) Special Fund

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(5) Revolving Fund

(6) Clearing Fund

**Management Comments. B.2.a.** Concur. Even though the guidance was not clear, as the audit report pointed out, this finding was not material as the net adjustment between entity and non-entity accounts was only approximately \$79 million against the total dollar value. GAFS-R posting logic was modified to properly categorize GLA 1010 for expenditure and receipt accounts with the proper attribute of entity, non-entity, appropriated fund, trust funds, special fund, and other fund types. We are on track to validate these modifications with August 2005 reporting in September 2005.

**Estimated Completion Date.** November 30, 2005 (Applies to B.2.a)

Point of Contact. Sylvia Taylor-Porter/ADGG/303-676-7750

**Management Comments. B.2.b. (1)-(6).** Non-Concur. The recommended categories of General Fund, Deposit Fund, and Clearing Account in accordance with Note 3.A. Funds Balance with Treasury, are not required attributes, and are in conflict with DoD FMR, Volume 6B, Chapter 10, "Notes to the Financial Statements," January 2002, Section 1005, "Note 3. Fund Balance With Treasury," states: "... disclose the assets by fund type (appropriated, revolving, trust, or in the other fund type category)." Specifically, the General Fund FBWT account has to be classified as appropriated, trust, and other fund type. The aforementioned items within the recommendation are in conflict with the DoD FMR as stated.

**Estimated Completion Date.** Not Applicable (Applies to B.2.b.)

Point of Contact. Sylvia Taylor-Porter/ADGG/303-676-7750

**Recommendation C.2.** We recommend that the Director of Defense Finance and Accounting Service Denver finalize their draft Standard Operating Procedures, "Journal Voucher Guidance for General Funds," December 21, 2004, and make the procedures applicable to journal voucher adjustments in the Defense Departmental Reporting System-Budgetary and Defense Departmental Reporting System-Audited Financial Statements. In addition, include the following requirements to provide:

- a. Applicable criteria to support the rationale for the journal voucher adjustment on the journal voucher or supporting documentation.
- b. Specific expenditure or receipt accounts affected by the journal voucher adjustment on the journal voucher or supporting documentation.

- 
- c. Calculation of the dollar amount of the journal voucher adjustment and references to supporting documentation.

**Management Comments. C.2.a.b.c.** Concur. This finding was not material as Journal Voucher narrative explanations can always be improved; however, this finding merely requests additional clarification of existing narratives. Journal Voucher Guidance for General Funds dated December 2004 was provided for use in a draft status because the division continues to fine tune guidance. The guidance does require supporting documentation to support journal vouchers. Draft guidance will be enhanced and finalized as recommended addressing the following criteria:

- a. Applicable criteria to support the rationale for the journal voucher adjustment on the journal voucher or supporting documentation.
- b. Specific expenditure or receipt accounts affected by the journal voucher adjustment on the journal voucher or supporting documentation.
- c. Calculation of the dollar amount of the journal voucher adjustment and references to supporting documentation.

**Estimated Completion Date.** November 30, 2005 (Applies to C.2. a., b., & c.)

Point of Contact. Sylvia Taylor-Porter/ADGG/303-676-7750

**Recommendation D.2.** We recommend that the Director of Defense Finance and Accounting Service Denver establish standard operating procedures for identifying the expenditure and receipt accounts that should be used in the calculation of Line 2.A., "Fund Balance per Treasury," of Note 3, "Fund Balance With Treasury."

**Management Comments. D.2.** Concur. This finding was not material as guidance being followed at the time was proper. This finding merely requests formalization of an SOP with revised OUSD guidance. OUSD (C) has clarified reporting requirements for Note 3, line 2A. DFAS-DE has implemented revised, clarified procedures provided by OUSD (C) for identifying the expenditure and receipt accounts that should be used in the calculation. Based on this revised guidance, which was not available at the time of audit, we shall establish Standard Operating Procedures to address these issues.

**Estimated Completion Date.** November 30, 2005 (Applies to D.2.)

Point of Contact. Sylvia Taylor-Porter/ADGG/303-676-7750

**Recommendation E.1.** We recommend that the Director of Defense Finance and Accounting Service Denver:

- 
- a. Develop tests to determine whether internal controls have been designed and implemented to prevent the material weaknesses identified in findings A, B, C, and D of this report.
  - b. Report the material weaknesses identified in findings A, B, C, and D of this report in their Annual Statement of Assurance until they are corrected.
  - c. Establish coordination procedures with Defense Finance and Accounting Service Headquarters to ensure consistent reporting of applicable material weaknesses between the Defense Finance and Accounting Service Denver Annual Statement of Assurance and the Defense Finance and Accounting Service Headquarters Annual Statement of Assurance.

**Management Comments. E.1.** Non-concur. As previously stated, none of the findings were proven to identify any material or substantive deficiencies. Therefore, we do not agree the audit report's findings A, B, C, or D provide any factual basis for reporting the issues mentioned as material weaknesses. Further reading the audit report, the reader would have to assume there is no effective or formalized internal control structure at DFAS Denver. However, the remaining recommended actions were already in place at the time of the audit and remain in place today. While any process and/or procedure can be improved, the implication with these recommendations is there was and is no formal or documented internal control structure in place at DFAS Denver. In 2002 the DFAS Denver Management Control Program (MCP) guidelines were published addressing the internal control program at DFAS Denver. These guidelines outline a formalized program requiring a general assessment of each assessable unit's control environment to include documenting management and application internal controls. The finalized results of each assessable unit's evaluation of their control environment are documented in an individual internal control inventory unique to that assessable unit. These inventories of internal controls then serve as the base line to perform internal control testing and the results of that testing are documented in formalized management certified summary matrices. The overall process of developing, monitoring, and testing of internal controls is then used to determine materiality and eventual reporting of formal material weaknesses, as determined by management, under the auspices of the Federal Managers' Financial Integrity Act (FMFIA).

The DoDIG audit team was provided the DFAS Denver 2002 MCP operating instructions during their review. In addition the 2004 and 2005 internal control inventories, testing matrices, and certification documents signed by the assessable unit managers for the areas under review were provided to the audit team. Finally, the DFAS Denver Management Control Program Office provided the audit team access to the e-portal project which contains the internal control documentation and evidential matter for all assessable units for the Air Force Accounting Business Line at DFAS Denver. The DFAS Denver MCP office then guided the audit team through the documentation furnished and the procedural guidelines published.

**Estimated Completion Date.** Not Applicable

Point of Contact. Dan Valdez, DFAS-ADN/DE, 303-676-7253

## **Team Members**

The Department of Defense Office of the Deputy Inspector General for Auditing, Defense Financial Auditing Service prepared this report. Personnel of the Department of Defense Office of Inspector General who contributed to the report are listed below.

Paul J. Granetto  
Patricia A. Marsh  
Douglas P. Neville  
Mark S. Henricks  
William W. Lemmon  
James H. Fleischman  
Jose J. Delino  
Thomas G. Daquano, Jr.  
William R. Fagerholm  
Cindy L. Gavura