

November 7, 2005



# Financial Management

## Report on the Foreign Military Sales Trust Fund Cash Management (D-2006-011)

Department of Defense  
Office of Inspector General

Constitution of  
the United States

A Regular Statement of Account of the Receipts and Expenditures of all public Money shall be published from time to time.

Article I, Section 9

### **Additional Copies**

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

### **Suggestions for Future Audits**

To suggest ideas for or to request future audits, contact Audit Followup and Technical Support at (703) 604-8940 (DSN 664-8940) or fax (703) 604-8932. Ideas and requests can also be mailed to:

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

DEPARTMENT OF DEFENSE

**hotline**

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

Send written complaints to: Defense Hotline, The Pentagon, Washington, DC 20301-1900  
Phone: 800.424.9098 e-mail: [hotline@dodig.osd.mil](mailto:hotline@dodig.osd.mil) [www.dodig.mil/hotline](http://www.dodig.mil/hotline)

### **Acronyms**

DCAS	Defense Cash Accountability System
DFAS	Defense Finance and Accounting Service
DFAS Denver	Defense Finance and Accounting Service, Denver Center
DIFS	Defense Integrated Financial System
DSCA	Defense Security Cooperation Agency
DSSN	Disbursing Station Symbol Number
FICS	Foreign Military Sales Integrated Control System
FMR	DoD Financial Management Regulation
FMS	Foreign Military Sales
MILDEP	Military Department



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

November 7, 2005

MEMORANDUM FOR DIRECTOR, DEFENSE FINANCE AND ACCOUNTING  
SERVICE

SUBJECT: Report on the Foreign Military Sales Trust Fund Cash Management (Report  
No. D-2006-011)

We are providing this report for review and comment. We performed this audit in response to a request from the Defense Security Cooperation Agency. We considered management comments on a draft of this report when preparing the final report.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The Defense Finance and Accounting Service concurred or partially concurred with all findings and recommendations; however, comments were partially responsive to the recommendations in Finding B. Therefore, we request that the Director, Defense Finance and Accounting Service, reconsider his position and provide additional comments in response to the final report on Finding B, Recommendations B.1, B.2 and B.3 by January 9, 2006.

If possible, please send management comments in electronic format (Adobe Acrobat file only) to [Aud.dfs@dodig.mil](mailto:Aud.dfs@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).

Questions should be directed to Byron B. Harbert at (303) 676-7392 (DSN 926-7392) or Mr. John W. Barklage at (303) 676-3298 (DSN 926-3298). See Appendix B 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, appearing to read "Paul J. Granetto", is positioned above the printed name.

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

## Department of Defense Office of Inspector General

Report No. D-2006-011

November 7, 2005

(Project No. D2004-D000FD-0039.000)

### The Foreign Military Sales Trust Fund Cash Management

#### Executive Summary

**Who Should Read This Report and Why?** This report should be read by the DoD Chief Financial Officer and personnel in the Defense Security Cooperation Agency and the Defense Finance and Accounting Service (DFAS) who are responsible for the management and day-to-day operations of the Foreign Military Sales Trust Fund. The report discusses how to improve controls and prevent abuse in this important program.

**Background.** The Defense Security Cooperation Agency directs, administers, and supervises the execution of the Security Assistance programs for the Department of Defense. Foreign Military Sales (FMS) is one of the Security Assistance programs. FMS includes government-to-government sales of Defense articles or Defense services from DoD stocks or through new procurements under DoD-managed contracts. The FMS customer is generally required to pay, in advance, amounts necessary to cover costs associated with the services or items purchased from DoD. The Department of the Treasury holds these advance payments in the Foreign Military Sales Trust Fund. The Trust Fund has total deposits of approximately \$11 billion and annually disburses approximately \$11 billion. DFAS performs the accounting, billing, disbursing, and collecting functions for this Security Assistance program.

**Results.** DFAS needs to improve internal control of the FMS cash management program. DFAS disbursing controls were inadequate to ensure that sufficient cash was available in applicable country accounts before making disbursements. Further, DFAS personnel did not properly and accurately post expenditure authority to country accounts. We estimate that DFAS disbursed between \$83 million and \$384 million in the second quarter FY 2004 without expenditure authority. Without the assurance that sufficient cash is available in applicable country accounts prior to disbursing, the use of the wrong countries' funds or U.S. Government funds could occur (finding A).

DFAS did not establish adequate audit trails to enable managers or auditors to verify disbursements. As a result, we were unable to determine the validity or accuracy of FMS disbursements and whether DFAS and Military Department personnel requested expenditure authority prior to disbursing FMS funds (finding B). See the Finding sections of the report for the detailed recommendations. We also reviewed the management control program as it related to cash management of the Foreign Military Sales Program. DFAS needs to improve the cash management procedures and ensure that there are adequate audit trails for disbursements.

**Management Comments and Audit Response.** The Director of Accounting Services, Defense Finance and Accounting Service, concurred or partially concurred with all findings and recommendations. On the first finding, the Director concurred with five

recommendations and partially concurred with one recommendation, stating that DFAS Denver now enforces a written policy from the Defense Security Cooperation Agency Comptroller directing that, without exception, expenditure authority is not to be approved pending drawdown or receipt of funds. The Director further stated that DFAS Denver has instituted a zero tolerance position on the lack of expenditure authority requests. When they determine that disbursements occurred without expenditure authority, DFAS Denver requires an explanation and course of action as mandated by the DoD Financial Management Regulation. The Director further stated that DFAS will also establish measurements for certifying officers to ensure that compliance to expenditure authority requirements are met.

The Director partially concurred with the second finding and concurred with all three recommendations, stating that DFAS does have adequate audit trails for disbursements, but the manner in which the information is supported is different than the methodology proposed by the audit and this support could be improved. The Director also agreed that the availability of the voucher number in the accounting system would improve the FMS audit trail. The DFAS proposed solution was to include the audit trail information as part of the Defense Cash Accountability System Phase V system improvement, scheduled for implementation in September 2007.

The DFAS comments were not fully responsive. We do not agree that an adequate audit trail exists to verify the disbursements recorded in the FMS Trust Fund accounting system; we believe an interim solution should be explored to implement an adequate audit trail before the Defense Cash Accountability System is implemented. DFAS Security Assistance personnel were unable to positively identify source documents for all the sample transactions. The absence of an adequate audit trail makes the FMS Trust Fund vulnerable to fraud, and this material internal control weakness should be corrected as soon as possible. DFAS should explore the requirements to add voucher number and disbursement date to the FMS accounting system and the systems that feed it. DFAS should then decide whether the interim change would be feasible and cost effective.

We request that the Director, DFAS, reconsider his position and provide comments to the final report on finding B and recommendations B.1, B.2 and B.3 by January 9, 2006. See the Finding section 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

---

<b>Executive Summary</b>	i
<b>Background</b>	1
<b>Objectives</b>	1
<b>Findings</b>	
A. Internal Control of Cash Management	2
B. Adequacy of Audit Trails	9
<b>Appendixes</b>	
A. Scope and Methodology	14
Management Control Program Review	14
Prior Coverage	15
B. Report Distribution	17
<b>Management Comments</b>	
Defense Finance and Accounting Service	19

---

## Background

The Arms Export Control Act of 1976, established in section 38, title 22, United States Code, as amended, gives the President authority to sell Defense articles and services to eligible foreign countries, generally at no cost to the U.S. Government. This is done through the Security Assistance programs authorized by the Foreign Assistance Act of 1961, as amended; the Arms Export Control Act of 1976, as amended; and annual appropriations acts for Foreign Operations, Export Financing and Related Programs.

The Defense Security Cooperation Agency (DSCA) directs, administers, and supervises the execution of all Security Assistance programs for the Department of Defense. Foreign Military Sales (FMS) is one of the major types of Security Assistance programs. FMS includes government-to-government sales of Defense articles or Defense services from DoD stocks or through new procurements under DoD-managed contracts. The FMS customer is generally required to pay, in advance, amounts necessary to cover costs associated with the services or items purchased from DoD. The Department of the Treasury holds these advance payments in the FMS Trust Fund. The Trust Fund has total deposits of approximately \$11 billion and annually disburses approximately \$11 billion. The Defense Finance and Accounting Service (DFAS) performs the accounting, billing, disbursing, and collecting functions for this Security Assistance program.

## Objectives

Our overall audit objective was to evaluate the cash management of the FMS Trust Fund. Specifically, we determined whether internal control was adequate to ensure that:

- sufficient cash was available in the applicable country account before expenditure authority was issued to a disbursing office,
- expenditure authority was posted promptly and accurately to the country's account, and
- changes to the country account balances were adequately supported.

We also reviewed the management control program as it related to the overall objective. See Appendix A for a discussion of the scope and methodology, our review of the management control program, and prior coverage related to the objectives.

---

## **A. Internal Control of Cash Management**

Internal control was not adequate to ensure that sufficient cash was available in applicable country accounts before FMS disbursements were made. This occurred because DFAS personnel did not post expenditure authority promptly to country accounts. Based on a statistical sample, we estimate that DFAS disbursed between \$83 million and \$384 million in the second quarter FY 2004 without expenditure authority. In addition, \$24,886 of one country's funds were used to pay another country's bill. FMS disbursements were made by numerous disbursing offices worldwide. DFAS personnel did not always obtain expenditure authority prior to disbursing because this required disbursing offices to do additional work, and there were no adverse consequences for those disbursing officers not obtaining expenditure authority. In addition, existing procedures allowed disbursing offices to obtain expenditure authority after FMS disbursements were made. Unless DFAS ensures that sufficient cash is available in applicable country accounts prior to disbursing from those accounts, the use of the wrong countries' funds or U.S. Government funds could occur.

### **Expenditure Authority**

Budget authority for U.S. Government appropriations provides the authority to obligate and disburse. However, budget authority for FMS provides the authority only to obligate. Expenditure authority, issued by DFAS Denver Center (DFAS Denver), authorizes disbursing offices to disburse FMS funds. Consequently, unless disbursing offices obtain expenditure authority before making FMS disbursements, the disbursements are unauthorized.

### **Termination Liability**

Termination liability is a reservation of funds in a country's account to ensure that the U.S. Government is protected in the event that a country defaults. DSCA determines amounts needed for each country account. The termination liability amount for each country must be on hand in either the Treasury or in an interest-bearing account controlled by DoD. DFAS is not authorized to make a disbursement if the disbursement would use any amount of the termination liability reserve without DSCA approval.

### **Criteria**

DoD 7000.14-R, "DoD Financial Management Regulation," (FMR) volume 15, "Security Assistance Policy and Procedures," April 2002, states that any disbursement from the FMS Trust Fund made by an organization other than



---

DFAS Denver can be made only after DFAS Denver issues expenditure authorization. The FMR also states that an adverse financial condition exists when expenditure authority is not obtained prior to disbursing FMS funds. The FMR requires that an adverse financial condition report be submitted to DFAS Denver when expenditure authority is not requested prior to disbursing. In addition, the FMR prohibits the use of one country's cash to pay for another country's bills, except when authorized by the country providing the cash.

## **Internal Control**

Internal control at DFAS was not adequate to ensure that sufficient cash was available in applicable country accounts before FMS disbursements were made. DFAS did not post expenditure authority promptly to country accounts.

We selected a stratified random sample of 400 FMS disbursements. DFAS officials could not provide documentation for 133 of those disbursements, because DFAS had not established an adequate audit trail for disbursements (see finding B). In addition, 35 of our sample items were adjustments that were commingled with disbursements in DFAS records. We examined the remaining 232 disbursements totaling \$545 million; 47 of those disbursements, totaling \$39.4 million, were made without expenditure authority. From our sample results, we estimate with 95 percent confidence that between \$83 million and \$384 million was disbursed in the second quarter of FY 2004 without expenditure authority, with \$233 million as the midpoint estimate. According to DFAS Denver records, at least \$229 million was disbursed in the second quarter FY 2004 without expenditure authority obtained prior to the disbursements; however, only \$28 million was reported to DSCA. DFAS Denver received only one adverse financial condition report, despite the high rate of unauthorized disbursements made.

Between April 2003 and March 2004, three FMS disbursements totaling \$26 million were made when adequate cash was not available in the applicable country accounts. In two instances, DFAS Denver used termination liability reserve for part or all of the disbursements, and in one instance, DFAS Denver used \$24,886 of another country's funds because the billed country had insufficient available cash.

Unauthorized FMS disbursements have been a long-standing problem at DFAS. In August 1996, the Director of DFAS issued a memorandum to all DFAS Centers that stated,

The expenditure authority must be requested for all FMS Trust Fund disbursements prior to issuing checks or making electronic funds transfer payments.

---

The memorandum also stated,

Effective immediately, we expect all disbursing officers to achieve a zero tolerance in obtaining FMS expenditure authority and in reporting valid disbursements by FMS country and case.

In May 2000, the Deputy Director of DFAS issued a memorandum to all DFAS Centers, which stated that expenditure authority requirements were not always met, and that the FMR required any disbursing activity that made unauthorized FMS disbursements to prepare an adverse financial condition report. The memorandum concluded with the statement,

In order to eliminate disbursement transactions processed without expenditure authority, the provisions of DoDFMR 7000.14-R shall be followed without exception.

Despite the two policy memorandums, DFAS disbursing offices continued to make unauthorized disbursements and, in only one instance did they submit an adverse financial condition report.

The Government Accountability Office issued Report FGMSD-79-33, "Centralization: Best Long-Range Solution to Financial Management Problems of the Foreign Military Sales Program," on May 17, 1979. The report cited FMS accounting and financial management problems, and included a recommendation to centralize the disbursing function.

In DoD IG, Audit Report No. 98-164, "Internal Controls and Compliance with Laws and Regulations for the Defense Security Assistance Agency Financial Statements for FY 1997," June 25, 1998, we reported that disbursing officers disbursed \$494 million in FY 1997 from the FMS Trust Fund without obtaining expenditure authority. DFAS has not taken sufficient action to correct this condition, which continues to exist.

## **Obtaining Expenditure Authority**

Disbursing offices worldwide made numerous FMS disbursements. Disbursing offices did not always obtain expenditure authority prior to making disbursements because this required disbursing offices to do additional work, and there were no adverse consequences for those disbursing officers not obtaining expenditure authority. In addition, existing procedures allowed disbursing offices to obtain expenditure authority after FMS disbursements were made.

Disbursing offices are identified by a Disbursing Station Symbol Number (DSSN). However, some disbursing offices had more than one DSSN. A total of 78 DSSNs disbursed FMS funds in the second quarter of FY 2004. DFAS Denver officials did not know how many actual disbursing offices existed among the 78 DSSNs. Some disbursing offices obtained expenditure authority through automated systems, while others used manual processes. For some disbursing offices, FMS disbursements were an abnormal type of disbursement. Most

---

disbursements at those offices were for DoD, which did not require obtaining expenditure authority. Disbursing personnel were not fully trained or motivated to make the additional effort to obtain expenditure authority prior to making FMS disbursements. Disbursing officers were not held accountable for the unauthorized disbursements they made. Although DFAS Denver notified disbursing officers of the requirement to submit adverse financial condition reports for all unauthorized disbursements, no enforcement mechanism was established.

DFAS Denver established procedures that allowed disbursing offices to circumvent the requirement to obtain expenditure authority prior to making disbursements. DFAS Denver allowed disbursing offices to obtain expenditure authority up to 15 days after the end of the month in which FMS disbursements were made. By allowing disbursing offices to obtain expenditure authority after disbursing, there was no incentive for disbursing offices to obtain expenditure authority prior to disbursement. During the second quarter of FY 2004, disbursing offices disbursed \$201 million without requesting expenditure authority until after the end of the accounting month.

## **Conclusion**

Current policies and procedures are inadequate to ensure that expenditure authority is always obtained before making FMS disbursements. When expenditure authority is not obtained before FMS disbursements are made, there is risk that the country may not have enough funds to cover the disbursement or that the country's termination liability reserve would be reduced. Using termination liability funds to pay bills places the U.S. Government at risk in the event that the country subsequently defaults on the sales agreement. If FMS Trust Fund monies are used to cover a deficient country's disbursement, other country accounts in the FMS Trust Fund are used to cover the disbursement, which violates the requirement that no country's money be used for another country's disbursements. DoD stewardship responsibility in maintaining accountability and control of all foreign country monies dictates the need to ensure that no country's monies be used to pay for another country's bills unless that country had agreed to the payment.

The two memorandums to disbursing offices from high-level DFAS managers had no effect on performance. Managing expenditure authority and implementing adequate controls is a very difficult and labor-intensive process because of the number of disbursing offices involved. DFAS could implement strong measures such as holding disbursing officials accountable, establishing tough penalties, and forcing disbursing office compliance. However, such measures would be exceedingly difficult to implement, would require additional management staff at DFAS Headquarters, and would require an excessive amount of resources to be expended at disbursing offices and DFAS Headquarters.

A more practical approach would be to establish a single disbursing office for FMS. All FMS disbursements would be made by the centralized disbursing office. Because personnel in the centralized disbursing office would process only

---

FMS disbursements, they would be fully knowledgeable of the requirement to obtain expenditure authority before making disbursements. Management of the FMS disbursing function would be greatly simplified and would be much more effective and efficient.

Until a centralized disbursing office can be established, DFAS needs to establish effective interim controls to ensure that disbursing offices always obtain expenditure authority before making FMS disbursements. DFAS Denver needs to immediately stop the practice of allowing disbursing officers 15 days after the end of the month of disbursement to obtain expenditure authority.

## **Management Comments on the Findings and Audit Response**

The Director of Accounting Services of the Defense Finance and Accounting Service stated that, although expenditure authority (EA) is an important control and a key management information tool, there are other controls in place to ensure the adequacy of client deposits. Management further acknowledged that strengthening the EA process controls will only serve to improve cash controls over the FMS Trust Fund, and that DFAS has initiated actions to improve these controls.

**Audit Response.** Expenditure authority is the key management control for ensuring that sufficient cash is available in a foreign country's account before disbursement is made. While the other controls are important, they are not totally reliable for ensuring that a country has sufficient funds when a disbursement is to be made.

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

### **A. We recommend the Director, Defense Finance and Accounting Service:**

#### **A.1. Implement adequate internal control to preclude Foreign Military Sales disbursements without expenditure authority.**

**Management Comments:** The Director of Accounting Services of the Defense Finance and Accounting Service concurred and stated they agree that DFAS must ensure that adequate internal controls are in place to ensure the EA is recorded for all FMS disbursements. The Director further stated that DFAS Denver now enforces a written policy from the DSCA Comptroller directing that, without exception, expenditure authority is not to be approved pending drawdown or receipt of funds. The Director also stated that DFAS Denver has instituted a zero tolerance position on the lack of EA requests. When EA and disbursements are compared at month-end, and a variance exists where disbursements occurred without EA, DFAS Denver requires an explanation and course of action as mandated by the DoD FMR. The Director stated that DFAS will also establish measurements for certifying officers to ensure that compliance to EA

---

requirements are met. To further ensure EA is properly recorded, DFAS will provide a memorandum to the DFAS Director of Policy and Requirements emphasizing the requirement to incorporate EA controls in the design and development of systems involved in the accounts receivable process. DFAS has also elevated this issue to the DFAS Joint Requirements Board, who agreed to initiate a Business Case Analysis to identify a short term solution to ensure EA is requested and recorded.

**A.2. Implement controls at Defense Finance and Accounting Service Denver to preclude personnel from using one country's funds to cover another country's disbursement.**

**Management Comments:** The Director of Accounting Services of the Defense Finance and Accounting Service concurred and stated that the individual and supervisor involved were counseled and additional training was provided. Management further stated that control and oversight was increased to include another level of approval to ensure that the supervisor approves the payments.

**A.3. Ensure that disbursing officers submit adverse financial condition reports for each unauthorized Foreign Military Sales disbursement made.**

**Management Comments:** The Director of Accounting Services of the Defense Finance and Accounting Service concurred and stated the activity responsible for requesting EA must prepare and submit an Adverse Financial Condition Report. The Director further stated that DFAS Denver has instituted a zero tolerance position on the lack of EA requests. When month-end variances exist where disbursements occurred without EA, DFAS Denver requires an explanation and course of action as mandated by the DoD FMR. In the event the EA is not requested, DFAS requires the disbursing and certifying officers to coordinate to ensure the AFC Report is prepared and submitted.

**A.4. Hold disbursing officers accountable for unauthorized disbursements made.**

**Management Comments:** The Director of Accounting Services of the Defense Finance and Accounting Service concurred and stated that the activity responsible for pulling EA should be held accountable for unauthorized disbursements. However, the Director stated that it is the certifying officer's responsibility to ensure EA is requested. DFAS has drafted a memorandum for issuance by the Deputy Chief Financial Officer, DoD, to reemphasize the requirement to request EA for all FMS Trust Fund disbursements, clarify EA responsibilities, establish the framework for responsibilities for obtaining EA, and delineate the reporting requirements and disciplinary action for failure to follow these requirements.

**A.5. Establish a single, centralized disbursing office to make all disbursements for Foreign Military Sales.**

**Management Comments:** The Director of Accounting Services of the Defense Finance and Accounting Service partially concurred and agreed that the

---

establishment of a centralized disbursing office to make all disbursements for FMS would allow centralized control of EA and would curtail unauthorized disbursements. The Director stated they will initiate a Business Case Analysis, which the DFAS Joint Requirements Board has agreed to oversee, to evaluate the development of a centralized FMS disbursing entity. The Director further stated that centralized disbursing is contingent upon the results of the study and coordination with all of the disbursing offices and payment certification activities.

**Audit Response:** Although the Director of Accounting Services of the Defense Finance and Accounting Service only partially concurred, we consider the comments responsive. The actions taken satisfy the intent of the recommendation. Additional comments are not required.

**A.6. Immediately stop the Defense Finance and Accounting Service Denver practice of allowing disbursing offices 15 days after the end of the month to obtain expenditure authority.**

**Management Comments:** The Director of Accounting Services of the Defense Finance and Accounting Service concurred and stated that DFAS Denver has stopped accepting after-the-fact EA requests.

---

## **B. Adequacy of Audit Trails**

DFAS did not have an adequate audit trail for disbursements. DFAS and Military Department (MILDEP) disbursing station personnel were unable to find supporting documentation for 133 of the 400 sampled transactions because transaction information necessary to identify the documentation was not available in the accounting system. This is a long-standing material weakness in DFAS that has been reported in three previous DoD IG reports since 1993. Without the supporting documentation, we were unable to determine the validity or accuracy of FMS disbursements. We were also unable to determine whether DFAS and MILDEP personnel requested expenditure authority prior to disbursing FMS funds.

### **Defense Integrated Financial System**

In order to determine if expenditure authority was being properly requested, we attempted to trace disbursement transactions from the Defense Integrated Financial System (DIFS) to their source documentation at the various disbursing stations to determine the date of disbursement. DIFS is the departmental-level central accounting system used by the DFAS Directorate for Security Assistance, formerly known as the Security Assistance Accounting Center, at DFAS Denver to account for funds in the FMS Trust Fund. Information entered into the central accounting system in the form of accounting transactions is based on a combination of transactions received from installation-level FMS Integrated Control Systems (FICS) and vouchers recorded at DFAS Denver as a result of billing or collection and disbursement activity. Accounting transactions are recorded in applicable proprietary, department-level, and installation-level general ledger accounts. This enables DFAS Denver to prepare required accountability and fund status reports for the FMS Trust Fund.

### **Criteria**

DoD Regulation 7000.14-R, the “DoD Financial Management Regulation,” volume 1, “General Financial Management Information, Systems, and Requirements,” chapter 3, “Accounting Systems Conformance, Evaluation, and Reporting,” May 1993, provides the key accounting requirements for DoD financial management systems. Key Accounting Requirement No. 8 states that in any compliant system, the financial transactions for which the system accounts must be adequately supported with pertinent documents and source records. The FMR, volume 6A, “Financial Reports Roles and Responsibilities,” March 2002, also requires DFAS to maintain a complete and documented audit trail to support the reports it prepares.

---

## Disbursement Audit Trails

DFAS did not have an adequate audit trail for disbursements. DFAS and MILDEP disbursing station personnel were unable to find supporting documentation for 133 of the 400 sampled transactions. DIFS maintained the summary records of FMS disbursements, but individual disbursements could not be traced from DIFS to records at disbursing stations. This is a long-standing material weakness in DFAS that has been reported in three previous DoD IG reports since 1993.

- In Report No. 93-123, “Consolidating Financial Statements of the Foreign Military Trust Fund – FY 1992,” June 24, 1993, we reported that DoD did not have adequate audit trails for FMS disbursements.
- In Report No. 96-187, “Internal Controls and Compliance with Laws and Regulations for the FY 1995 Financial Statements of the Defense Security Assistance Agency,” June 28, 1996, we reported that DFAS Denver did not have reasonably accessible audit trails for FMS disbursements.
- In Report No. 98-164, “Internal Controls and Compliance with Laws and Regulations for the Defense Security Assistance Financial Statements for FY 1997,” June 25, 1998, we reported that DFAS did not have clearly established audit trails for FMS disbursements.

In response to our recommendation to implement adequate FMS disbursement audit trails in Report No. 98-164, the DoD Deputy Chief Financial Officer stated that an audit trail for disbursements would be established, documented, and tested by September 30, 1998. However, 6 years later, audit trails for FMS disbursements remain inadequate.

## Data Requirements

DFAS and MILDEP disbursing station personnel were unable to find supporting documentation because transaction information required to identify the documentation was not available in the accounting system. To find the supporting documentation at the disbursing stations, personnel need the individual disbursement transaction voucher number and disbursement date within DIFS. Although DIFS has data fields for this information, the voucher number and disbursing date are not the actual transaction data recorded in the field accounting systems. These data are not being processed to DIFS for most disbursement transactions.

In addition, all of the disbursing offices did not accurately record FMS disbursements, and DIFS did not have edit checks on the DSSN data field. Because DIFS does not have edit checks on this data, the system accepted any information that was recorded in the DSSN field. There were 37 DSSNs recorded in DIFS that the DFAS Denver staff could not identify.



---

DFAS Denver officials stated the disbursement voucher number and disbursement date were not needed in DIFS because that information was available in the MILDEP feeder systems. However, DFAS and MILDEP field personnel could not locate documentation supporting disbursements without the voucher number and disbursement date. In addition, DFAS Denver officials also contended that validating the DSSN data would be labor intensive, time consuming, and not cost-effective when you look at the number of invalid DSSNs.

## **Conclusion**

Without supporting documentation, we were unable to determine the validity or accuracy of FMS disbursements. Additionally, we could not determine whether personnel were processing expenditure authority as required by the regulations.

Because we could not locate supporting documentation for all FMS disbursements, we could not determine whether expenditure authority was obtained before the disbursements were made or whether cash was available in applicable country accounts. The inability to determine whether disbursements were properly recorded adversely affects the ability of DFAS and DSCA to manage foreign country cash. Although we reported this finding in three previous audit reports since 1993, DFAS has still not taken sufficient action to establish adequate audit trails for FMS disbursements.

DIFS is the accounting system for cash management of the FMS Trust Fund. As such, the FMR requires that DIFS have an audit trail that allows auditors to ensure that transactions are properly accumulated and recorded in all accounts. The solution to the audit trail problem is not solely within DIFS. Changes may also need to be made to existing MILDEP and DFAS feeder systems to provide the data needed to establish an adequate audit trail. While DFAS has proposed modifications to DIFS, no changes have been made to date.

## **Management Comments on the Finding and Audit Response**

The Director of Accounting Services of the Defense Finance and Accounting Service partially concurred with the finding and stated DFAS does have adequate audit trails for disbursements, but that the manner in which the information is supported is different than the methodology proposed by the audit, and this support could be improved. The Director stated that since the audit trail weakness was first identified by the DoDIG, the DoD has implemented numerous systems and process enhancements that enable DFAS to establish adequate audit trails and achieve relational integrity to support the assertion process. The Director also stated that the voucher number data currently is not carried from the source documents and systems to DIFS, and agreed that the availability of the voucher number in the accounting system would improve the FMS audit trail. Management's proposed solution was to include the audit trail information as part of the Defense Cash Accountability System (DCAS) Phase V system improvement, scheduled for implementation in September 2007. The Director

---

stated that, with the implementation of the DCAS Phase V, DFAS and DoD components will ensure that all critical document requirements are included in the system designs and the voucher numbers are carried from the source document to DIFS or its replacement system.

**Audit Response.** The DFAS comments were not fully responsive. We do not agree that an adequate audit trail exists to verify the disbursements recorded in the FMS Trust Fund accounting system; we believe that an interim solution should be explored before the Defense Cash Accountability System is implemented. DFAS Security Assistance personnel were unable to positively identify source documents for all the sample transactions. The absence of an adequate audit trail makes the FMS Trust Fund vulnerable to fraud, and this material internal control weakness should be corrected as soon as possible. We think DFAS should explore other methods to add voucher number and disbursement date to the FMS accounting system and the systems that feed it prior to the DCAS Phase V implementation. DFAS should then decide whether the interim change would be feasible and cost effective.

We agree that since the DoDIG first reported the audit trail weakness in 1993, the DoD has implemented numerous systems and process enhancements. However, none of these enhancements or new systems has established the link from the source document to the accounting system record that is required by the DoD FMR. DFAS personnel attempted to trace the sampled disbursements by matching customer, disbursing office, and disbursement amount during the same month. This was a cumbersome and time-consuming process that did not result in positive identification of the sampled disbursement. For one of those sampled items, 165 disbursements were made during the same month, for the same customer, in the exact same amount. An adequate disbursement trail would enable managers and auditors to readily trace a transaction from an identifying number or code that would provide a link between the accounting system (DIFS) and the disbursement record. The voucher number that disbursing offices assign each disbursement could serve this purpose. When reporting systems provide DIFS the voucher number, the positive link needed for an adequate audit trail would be created.

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

**We recommend the Director, Defense Finance and Accounting Service, establish and document an adequate audit trail for Foreign Military Sales disbursements. In determining how to establish the audit trail, the Director, Defense Finance and Accounting Service should:**

**B.1. Consult with appropriate Defense Finance and Accounting Service disbursing officers and military department financial managers.**

**Management Comments:** The Director of Accounting Services of the Defense Finance and Accounting Service concurred, but referred to the partial concurrence statement in his comments on the finding. The Director stated that

---

the appropriate DFAS disbursing officers and military department financial managers will be consulted for the establishment of the audit trail under DCAS Phase V.

**Audit Response:** Management comments are partially responsive. We do not agree that an adequate audit trail exists to verify the disbursements recorded in the FMS Trust Fund accounting system; an interim solution should be explored before DCAS Phase V is completed.

**B.2. Identify all changes needed to the Defense Integrated Financial System, to other Defense Finance and Accounting Service systems, and to military department systems.**

**Management Comments:** The Director of Accounting Services of the Defense Finance and Accounting Service concurred, but referred to the partial concurrence statement in his comments on the finding. The Director stated that DCAS Phase V will be the mechanism for improving the audit trails.

**Audit Response:** Management comments are partially responsive. We do not agree that an adequate audit trail exists to verify the disbursements recorded in the FMS Trust Fund accounting system; an interim solution should be explored before DCAS Phase V is completed.

**B.3. Ensure the prompt implementation of changes needed to all applicable systems.**

**Management Comments:** The Director of Accounting Services of the Defense Finance and Accounting Service concurred, but referred to the partial concurrence statement in his comments on the finding. The Director stated that DCAS Phase V will be implemented for all DoD Components by September 30, 2007.

**Audit Response:** Management comments are partially responsive. We do not agree that an adequate audit trail exists to verify the disbursements recorded in the FMS Trust Fund accounting system; an interim solution should be explored before DCAS Phase V is completed.

We request the Director, DFAS, to reconsider his position and provide comments to the final report by January 9, 2006.

---

## Appendix A. Scope and Methodology

DSCA requested an audit of cash management of the FMS Trust Fund. We reviewed the guidance used for the execution of the FMS Trust Fund as well as the Congressional language that established the FMS Trust Fund. Specifically, we reviewed: The Arms Export Control Act of 1976, established in section 38, title 22, United States Code as amended, and annual appropriations acts for Foreign Operations, Export Financing and Related Programs; The Financial Management Regulation, volume 15; and The Security Assistance Management Manual. We reviewed the procedures and processes involved in Cash Management of the FMS Trust Fund. We interviewed personnel and gathered information from the Director for Security Assistance, DFAS Denver.

A random sample of 400 transactions was taken from a universe of 72,137 Foreign Military Sales disbursements for the second quarter of FY 2004. The universe was composed of both positive and negative values with an absolute value of \$4.4 billion. The population was divided into six strata by dollar value, three for positive values and three for negative values. By using the sample results, we projected the net disbursement amount without expenditure authority for the second quarter for FY 2004. During the sample review period we gathered data and conducted telephone interviews with personnel at various DFAS disbursing offices.

We performed this audit from December 2003 through November 2004 in accordance with generally accepted government auditing standards.

**Use of Computer-Processed Data.** We used reports generated from the Defense Integrated Financial System (DIFS) to aid us in obtaining our sample, but we did not rely on the information in DIFS to support our findings. DIFS data may be unreliable. As information is fed into DIFS by various feeder systems data are consolidated, and vital information is lost. This is discussed in finding B.

**Use of Technical Assistance.** The Technical Director and statisticians in the Quantitative Methods Division, DoD OIG designed and selected a statistical sample to determine the amount of expenditure authority that was not requested prior to disbursement. The statistician projected the results of the testing for 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 Defense Financial Management high-risk area.

### 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 management controls over the FMS Trust Fund program. Specifically, we reviewed DFAS Denver's management controls over the corporate cash management. We also reviewed management's self-evaluation application to those controls.

**Adequacy of Management Controls.** We identified material management control weaknesses for DFAS Denver as defined by DoD Instruction 5010.40. DFAS Denver management controls over cash management for the FMS Trust Fund are not adequate to ensure that sufficient cash was available in applicable country accounts before FMS disbursements were made. DFAS did not post expenditure authority promptly to country accounts. Additionally, DFAS Denver did not have an adequate audit trail for FMS disbursements. Recommendations A.1. through A.6. and B.1. through B.3., if implemented, will improve cash management procedures and ensure that there are adequate audit trails. A copy of the report will be provided to the senior official responsible for management controls in DFAS Denver.

**Adequacy of Management's Self-Evaluation.** DFAS Denver identified corporate cash management as an assessable unit. However, in its evaluation, DFAS Denver officials did not identify the specific material management control weaknesses identified by the audit because those officials did not consider the weaknesses to be material. However, management did identify weaknesses in the Fund Balance with Treasury process as material in the most recent report.

## Prior Coverage

No prior coverage has been conducted on Foreign Military Sales Trust Fund Cash Management during the last 5 years. However, the Department of Defense Inspector General has issued three reports discussing lack of audit trails for disbursements (finding B). Additionally, the most recent report also addresses expenditure authority (finding A). Unrestricted DoD IG reports can be accessed at <http://www.dodig.mil/audit/reports>.

## DoD IG

DoD IG Report No. D-1998-0164, "Internal Controls and Compliance with Laws and Regulations for the Defense Security Assistance Agency Financial Statements for FY 1997," June 25, 1998

DoD IG Report No. D-1996-0187, "Internal Controls and Compliance with Laws and Regulations for the FY 1995 Financial Statements of the Defense Security Assistance Agency," June 28, 1996

---

DoDIG Report No. D-1993-0123, "Consolidating Financial Statements of the Foreign Military Sales Trust Fund – FY 1992," June 24, 1993

---

## **Appendix B. 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**

Auditor General, Department of the Army

### **Department of the Navy**

Naval Inspector General  
Auditor General, Department of the Navy

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

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

### **Other Defense Organizations**

Director, Defense Finance and Accounting Service  
Director, Defense Security Cooperation Agency

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

Office of Management and Budget

---

## **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 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



# Defense Finance and Accounting Service Comments

Final Report  
Reference

Final Report  
Reference



DEFENSE FINANCE AND ACCOUNTING SERVICE  
CLEVELAND  
1240 EAST NINTH STREET  
CLEVELAND, OH 44189



October 7, 2005

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

SUBJECT: "Foreign Military Sales Trust Fund Cash Management,"  
(D-2004FD-0039) dated March 2, 2005

Our response to the request for follow-up comments to the subject audit is attached. The  
point of contact is Mr. Jerry Shea, (703) 601-3021 or DSN 329-3021.

L. J. Krushinski  
Director, Accounting Services

Attachment:  
As stated

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

**DFAS Management Response  
to  
Department of Defense  
Office of Inspector General**

**Draft Report of a Proposed Report**

**The Foreign Military Sales Trust Fund  
Cash Management**

**General Management Comments**

**(Project D2004FD-0039)**

**Finding A: Internal Control of Cash Management:**

The Foreign Military Sales (FMS) program must operate at no profit and no loss to the United States Government (USG). Accordingly we bill the foreign purchasers in advance of anticipated performance and implement a variety of controls to ensure that we have customer cash on hand in the FMS Trust Fund (FMSTF). Although Expenditure Authority (EA) is an important control, as well as a key management information tool, there are other cash controls in place to ensure the adequacy of client deposits. Strengthening EA process controls will only serve to improve cash controls over the FMSTF. DFAS has initiated actions to improve those controls.

Although the DODIG conducted a comprehensive review of the EA process, the audit defined as a cash control audit did not address those other controls and processes that in conjunction with the EA ensure the adequacy of customer cash. Although we partially concur as delineated below, and are committed to improve the EA process, we believe additional controls are in place enabling us to ensure that client cash is sufficient prior to EA being issued and disbursements being made. These controls include comprehensive cash forecasting, analysis of disbursement trends and the development of working capital requirements that enable us to bill the customers and draw funds from financial institutions in sufficient amounts to ensure cash sufficiency. In addition we reserve cash amounts within the FMSTF for projected reimbursements to USG appropriations and to safeguard the USG in the event of customer default. By exercising these controls in concert with EA, we ensure that a cash shortfall is an extraordinarily rare situation. Strengthening the EA will further secure FMSTF cash and we have and will continue our improvement efforts.

**Management Comments  
(Project D2004FD-0039)****Response to Recommendations****Recommendation A.1.**

We recommend the Director, DFAS: Implement adequate internal control to preclude FMS disbursements without Expenditure Authority.

**Management Comments.**

Concur. We agree that DFAS must ensure that adequate internal controls are in place to make certain EA is pulled for all FMS disbursements. As the central site responsible for the authorization of EA, DFAS-Denver now enforces a written policy from the current DSCA Comptroller that directs EA is not approved pending drawdown or receipt of funds, without exception even though EA denial may result in increase Prompt Pay Interest. Since the initial findings from this audit, DFAS-DE/ADYMA has instituted a zero tolerance position on the non-requesting of EA. When the EA and disbursements are compared at month-end and a variance exists where disbursements occurred without EA, DFAS-DE/ADY requires an explanation and course of corrective action as mandated in the Department of Defense Financial Management Regulation (DODFMR). In addition, DFAS will establish measurements for certifying officers to ensure compliance of EA requirements are met. DFAS will provide a memorandum to the DFAS Director of Policy and Requirements (draft attached) emphasizing the requirement to incorporate EA controls in the design and development of systems involved in the accounts receivable process. In addition the need to improve was elevated to DFAS Joint Requirements Board (JRB) to explore and identify a short term solution to ensure that EA is pulled. The charter of the JRB identifies themselves as the committee within DFAS that is responsible for the coordination of all interfacing system development and implementation within DFAS. At the last quarterly JRB meeting, the JRB agreed to initiate a Business Case Analysis (BCA) to address this short term solution, as well as the centralization of FMS Disbursing as recommended by the DODIG. DFAS Denver is currently working with the JRB to develop a schedule for the BCA.

However, DODIG must be aware that the use of multiple systems for certifying and disbursing creates certain problems with respect to timing. Often, a certifying officer will get EA for a certain month but the disbursement processes the next month. While technically this is a violation of the EA controls and is reported as a discrepancy, the FMSTF is not left unprotected. The BCA review will also look at EA processing, particularly those processes that are automated, to identify additional controls and ways to mitigate the reporting timing problem. Again, we are currently working with the JRB to develop a schedule for the BCA. A Plan of Actions and Milestones will be developed.

**Estimated Completion Date.** October 31, 2005

**Point of Contact.** Vicki George, ADYMA, 303-676-6006

**Recommendation A.2.**

We recommend the Director, DFAS: Implement controls at DFAS-Denver to preclude personnel from using one country's funds to cover another country's disbursement.

**Management Comments.**

Concur. Circumstance was confirmed as isolated to one instance. Individual and supervisor were counseled and additional training was provided. Management control and oversight was increased to include another level of approval to ensure that the supervisor approves payments.

**Completion Date.** March 31, 2005

**Point of Contact.** Vicki George, ADYMA, 303-676-6006

**Recommendation A.3.**

We recommend the Director, DFAS: Ensure that disbursing officers submit adverse financial condition reports for each unauthorized FMS disbursement made.

**Management Comments.**

Concur. We concur that the activity responsible for pulling EA must prepare and submit an Adverse Financial Condition (AFC) Report. Since the initial findings from this audit, DFAS-DE/ADYMA has instituted a zero tolerance position on the non-requesting of EA. When the EA and disbursements are compared at month-end and a variance exists where disbursements occurred without EA, DFAS-DE/ADY requires an explanation and course of corrective action and submission of the AFC report as mandated in the DODFMR. In most instances the certifying officer has the responsibility of requesting EA. In the event EA is not pulled, the disbursing and certifying officers must coordinate to ensure the AFC Report is prepared and submitted. Each month, DFAS-Denver provides EA/Disbursement Comparison Reports to all of the disbursing activities to notify them of discrepancies, along with a notification that an AFC Report is to be submitted for discrepancies identified by the responsible activity.

**Completion Date.** July 1, 2005

**Point of Contact.** Vicki George, ADYMA, 303-676-6006

**Recommendation A.4.**

We recommend the Director, DFAS: Hold disbursing officers accountable for unauthorized disbursements made.

**Management Comments.** Concur. We agree that the activity responsible for pulling EA should be held accountable for unauthorized disbursements. However we feel it is the certifying officer's responsibility to ensure EA is pulled. In compliance with the DODFMR, and reaffirmed by prior memorandums signed by DFAS Directors, DFAS requests an AFC Report for all unauthorized disbursements, defining problem causes and corrective action. We have drafted a memorandum (copy attached) for issuance by the Deputy Chief Financial Officer, DOD to re-emphasize the requirement to pull expenditure authority for all FMSTF disbursements, clarify EA responsibilities, establish the framework for holding the certifying officer responsible for obtaining EA, and delineate the reporting requirements and associated disciplinary action for failure to pull EA. The draft memorandum for the Deputy Chief Financial Officer (DCFO) was provided to the office of the Director of Policy at DFAS Arlington for review and coordination. A new Estimated Completion Date was established to allow coordination with the DOD Components engaged in FMS, prior to signature by the DCFO. Following is a Plan of Actions and Milestones for this action:

<u>Action Description</u>	<u>OPR</u>	<u>ECD</u>	<u>Status</u>
Draft DCFO Memo sent to DFAS-AR for coordination	ADYCOIDE	09/19/05	Completed
Begin Electronic Coordination for DCFO Memo	ADYCOIDE	09/30/05	
Electronic Coordination for DCFO Memo	ADYCOIDE	10/31/05	
Memorandum signed out by DCFO	OUSD(C)	11/30/05	

**Completion Date or Estimated Completion Date:** November 30, 2005

**Point of Contact:** Thomas Zacchini, ADYCO, 303-676-7924

**Recommendation A.5.**

We recommend the Director, DFAS: Establish a single, centralized disbursing office to make all disbursements for FMS.

**Management Comments.**

Partially Concur. We agree that the establishment of a single, centralized disbursing office to make all disbursements for FMS would allow us to centralize EA at one location and curtail unauthorized disbursements without EA. We will initiate a BCA to explore and evaluate the development of a centralized FMS disbursing entity. Centralizing disbursing is contingent upon the results of our study and coordination with all of the disbursing offices and payment certification activities. At the last quarterly JRB meeting, the JRB agreed to oversee the BCA to address centralizing FMS disbursing and we are currently working with the board to develop a schedule for the BCA. A Plan of Actions and Milestones will be developed.

**Estimated Completion Date.** October 31, 2005

**Point of Contact.** Kathy Dee, ADYC, 303-676-6170

**Recommendation A.6.**

We recommend the Director, DFAS: Immediately stop DFAS-Denver's practice of allowing disbursing offices 15 days after the end of the month to obtain EA.

**Management Comments.**

Concur. DFAS-Denver has stopped accepting after-the-fact EA requests.

**Completion Date.** March 31, 2005

**Point of Contact.** Vicki George, ADYMA, 303-676-6006

**Finding B: Adequacy of Audit Trails**

Partially Concur: DFAS does have adequate audit trails for disbursements. However, the manner in which the information is supported is different than the methodology proposed by the audit and could be improved. Since the audit trail weakness was first identified by the DODIG, the DOD has implemented numerous system and process enhancements that enabled DFAS to establish adequate audit trails and achieve relational integrity to support the DOD assertion process. In addition these improvements enabled the DODIG, with the assistance of the DFAS FMS staff, to track disbursement transactions in a secondary sample to the source documents with a much greater degree of success. We agree with the IG that the audit trail is sometimes cumbersome and that further improvement is desirable. Specifically, voucher number data is not carried from the source documents and systems to the DIFS, and the availability of that data would further improve the FMS audit trail.

The Department's overarching strategy to improve cash accounting will address voucher number traceability. This audit trail information will be provided as part of the Defense Cash Accountability System (DCAS) Phase V. As briefed by the DCAS Project Management Office, DCAS Phase V is scheduled for implementation September 2007. As the DCAS Phase V is finalized, DFAS and other DOD components will ensure that all the critical document requirements will be included in the system designs, and confirming that the associated audit trails are enhanced by ensuring the voucher number is carried from the source document to DIFS or its replacement system. The modification of any existing systems which interface both directly or indirectly to the DIFS will be a product of DCAS Phase V. The scheduled implementation of DCAS Phase V will obviate any separate requirement to modify existing systems which interface both directly or indirectly to the DIFS to contain voucher number identification from disbursing to eventual acceptance in the accounting records.

The DIFS audit trail does not feed FMSTF CFO reports, therefore the DIFS audit trail finding will not impact CFO reporting. However, we concur that the improvement of audit trails will serve to further strengthen our ability to control FMSTF cash resources, and those enhancements to DOD cash processes are presently in development.

**Recommendation B.1.**

In determining how to establish the audit trail, the Director, DFAS should:  
Consult with appropriate DFAS disbursing officers and military department financial managers.

**Management Comments.**

Concur See Partial-concurrence statement for the Recommendation B. The appropriate DFAS disbursing officers and the military department financial managers will be consulted for the establishment of the audit trail under DCAS Phase V.

**Estimated Completion Date.** September 30, 2007

**Point of Contact.** Stephen Wilson, ADYM, 303-676-6006



**Recommendation B.2.**

In determining how to establish the audit trail, the Director, DFAS should:  
Identify all changes needed to the DIFS, to other DFAS systems, and to military department systems.

**Management Comments.**

Concur. See Partial concurrence statement for the Recommendation B. DCAS Phase V will be the mechanism for improving the audit trails

**Estimated Completion Date.** September 30, 2007

**Point of Contact.** Stephen Wilson, ADYM, 303-676-6006

**Recommendation B.3.**

In determining how to establish the audit trail, the Director, DFAS should:  
Ensure the prompt implementation of changes needed to all applicable systems.

**Management Comments.**

Concur See Partial concurrence statement for the Recommendation B. The DCAS Phase V will  
be implemented for all DOD Components by September 30, 2007.

**Estimated Completion Date.** September 30, 2007

**Point of Contact.** Stephen Wilson, ADYM, 303-676-6006

DFAS-AD/DE

MEMORANDUM FOR DIRECTOR, POLICY AND REQUIREMENTS

SUBJECT: Foreign Military Sales (FMS) Trust Fund Expenditure Authority  
Requirements

The attached memorandum from the Deputy Chief Financial Officer, Department of Defense, reemphasized the requirement for ensuring that any expenditure, including expenditure adjustments, from the FMS Trust Fund shall be made only pursuant to an expenditure authorization (EA). EA is a critical FMS cash control needed to maintain the integrity of the FMSIF. Accordingly it is essential that the DFAS ensure that EA control requirements are incorporated into the design and development of the systems that will comprise target architecture for DOD financial management. Specifically these requirements will be built into the systems that will perform accounts payable/payment certification functions so as to make certain that EA is obtained prior to any disbursement and that EA is pulled in the same month as the ensuing expenditure. DOD's objective is to have an airtight system of internal controls to ensure the EA requirements is met.

If you have any questions or require any assistance, my point of contact for FMS Trust Fund matters is Mr. Greg Keiling, DFAS-ADY/DE.

Richard J. Anderfuren  
Director, Accounting Business Line Air Force

Attachment: DCFO Memorandum

CC: Jeff Yokel, Chair, Joint Requirements Board

Comptroller

MEMORANDUM FOR DIRECTOR DEFENSE FINANCE AND ACCOUNTING SERVICE

DIRECTORS, DEFENSE AGENCIES

COMPTROLLER, DEPARTMENT OF THE ARMY

COMPTROLLER, DEPARTMENT OF THE NAVY

COMPTROLLER, DEPARTMENT OF THE AIR FORCE

DIRECTOR, DEPARTMENT OF DEFENSE INSPECTOR GENERAL

SUBJECT: Foreign Military Sales (FMS) Trust Fund Expenditure Authority (EA)  
Requirements

The purpose of this memorandum is to establish accountability for the responsibility of ensuring Expenditure Authority (EA) is pulled prior to all FMS disbursements. Further, this memorandum will clarify roles and responsibilities, and delineate the reporting requirements and associated disciplinary action for failure to pull EA. Service organizations and Defense Agencies will be responsible for ensuring these responsibilities are implemented and administrative actions are taken as appropriate.

The Department of Defense Financial Management Regulation (DODFMR), Volume 15, paragraph 060101, states "Any disbursement of Trust fund cash by an organization other than the Security Assistance Accounting Center (SAAC) (now DFAS-ADY/DE) shall be made only pursuant to an expenditure authorization." EA is also required for expenditure adjustments. An expenditure authorization is not required for disbursements of FMSTF administrative funds.

The primary responsibility for obtaining the expenditure authorization rests with the certifying officer, who shall request EA from the DFAS-ADY/DE or interactively draw EA from the Defense Integrated Financial System (DIFS). The EA must be obtained in the same calendar month the ensuing expenditure will be made. In the event the expenditure will not be made in that same month, EA will be returned and obtained in that subsequent month.

The DODFMR, Volume 15, paragraph 021202, defines adverse financial conditions for the FMSTF to include when reports indicate "expenditure authority is not requested prior to disbursing." When reports indicate an adverse financial condition, the responsible activity will prepare a report of Adverse Financial Condition (AFC) in the format shown in DoDD 7200.1 and will submit that report to DFAS-ADY/DE.

A military member or civilian employee who is responsible for ensuring EA is obtained prior to disbursements and fails to do so may be subject to administrative disciplinary action. For a civilian employee this may include oral or written admonishment or reprimand. A military member may be subject to appropriate administrative discipline. Disciplinary action shall be administered on a case-by-case basis as determined by the appropriate authority. The level of discipline administered shall be commensurate with the record of the person responsible, their level of experience and the degree and level of responsibility of the individual. Any mitigating circumstances shall also be considered.

I will hold each Defense Component engaged in FMS payment certification accountable for obtaining EA and will, in turn hold your FMS activities equally accountable.

This policy is effective immediately, and changes to existing policy will be included in the next update of the DODFMR, Volume 15.

Theresa McKay  
Deputy Chief Financial Officer

## **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  
Brice Harbert  
John Barklage  
Mary Reynolds  
Kevin Roths  
Joshua Harcharik  
Mike Heers  
Catherine Bird  
Ann Thompson  
Erin Hart  
Frank Sonsini  
Lusk F. Penn  
Dharam Jain