Report No. D-2008-034 January 3, 2008

Inspector General

United States Department of Defense

Financial Management at the Defense Security Service

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 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 the Office of the Deputy Inspector General for Auditing at (703) 604-9142 (DSN 664-9142) or fax (703) 604-8932. Ideas and requests can also be mailed to:

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

DEPARTMENT OF DEFENSE hotline

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

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

Acronyms

DSS	Defense Security Service
FAR	Federal Acquisition Regulation
FM	Financial Management
FMR	Financial Management Regulation
MIPR	Military Interdepartmental Purchase Request
NISP	National Industrial Security Program
OPM	Office of Personnel Management
PSI	Personnel Security Investigation

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

January 3, 2008

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR INTELLIGENCE
DIRECTOR, DEFENSE SECURITY SERVICE

SUBJECT: Report on Financial Management at the Defense Security Service (Report No. D-2008-034)

We are providing this report for review and comment. We performed this audit in response to a request from the Director, Defense Security Service. This report discusses a potential violation of the Antideficiency Act. In accordance with DoD Regulation 7000.14-R, "Financial Management Regulation," volume 14, chapter 3.C., action to review the potential violation must be initiated within 10 days.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. The Office of the Under Secretary of Defense for Intelligence and the Defense Security Service did not provide comments to the draft report. Therefore, we request the Director, Defense Security Service provide comments on Recommendation 1. and the Office of Under Secretary of Defense for Intelligence provide comments on Recommendation 2. by February 4, 2008.

If possible, please send management comments in electronic format (Adobe Acrobat file only) to AudROS@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 Ms. Kimberley A. Caprio at (703) 604-9202 (DSN 664-9202) or Ms. Rhonda L. Ragsdale at (703) 604-9347 (DSN 664-9347). See Appendix E for the report distribution. The team members are listed inside the back cover.

By direction of the Deputy Inspector General for Auditing:

Wanda A. Scott

Wanda A. Scott
Assistant Inspector General
Readiness and Operations Support

Department of Defense Office of Inspector General

Report No. D-2008-034 **January 3, 2008**
(Project No. D2006-D000LC-0230)

Financial Management at the Defense Security Service

Executive Summary

Who Should Read This Report and Why? The Under Secretary of Defense (Comptroller)/Chief Financial Officer; the Under Secretary of Defense for Intelligence; the Director, Defense Security Service and the DSS Comptroller should read this report. The report discusses difficulties the Defense Security Service experienced identifying and managing financial requirements and complying with appropriation law and regulations.

Background. The Defense Security Service is the DoD organization responsible for providing DoD and other Federal Government agencies with a full range of security support services. On January 24, 2003, the Deputy Secretary of Defense and the Director of the Office of Personnel Management agreed to transfer the personnel security investigation function from the Defense Security Service to the Office of Personnel Management. In February 2005, the Defense Security Service transferred the investigation function, including 1,800 personnel security investigation positions and $33.8 million, to the Office of Personnel Management. The Defense Security Service retained responsibility for managing and funding personnel security investigations for contractor personnel. In June 2006, the Director of the Defense Security Service requested that we review the agency's financial management practices.

The Financial Management Division of the Defense Security Service has five branches: Budget Formulation, Budget Execution, Accounting, Performance Improvement, and Audit Readiness. The Comptroller, with the assistance of these five branches, is responsible for the agency's financial management functions, including enforcing internal controls to prevent Antideficiency Act violations and ensuring that resources are used efficiently and effectively.

Results. The Defense Security Service has taken steps to improve its financial management functions, but experienced difficulties in managing some aspects of financial management from FYs 2002 through 2007. The Defense Security Service should develop, implement, and monitor management controls to accurately estimate the cost of personnel security investigations; properly manage financial functions including obligations, accounts receivable, and contracting actions; and comply with regulations and appropriation laws. In addition, the Defense Security Service should initiate a preliminary review to determine whether it violated the Antideficiency Act by incorrectly using appropriated funds, and fill key financial management positions. While the Defense Security Service develops, implements, and monitors management controls, the Under Secretary of Defense for Intelligence should monitor financial management functions at the Defense Security Service. As the Defense Security Service continues making changes to its financial management practices and develops a more stable structure, it will be able to prepare supportable budget estimates and requests and ensure that it has adequate resources to perform its critical missions.

We identified a material internal control weakness. Defense Security Service did not have a system of management controls over some financial management practices to ensure sound business practices were performed and financial regulations were met. Implementing Recommendation 1. would improve the financial management process. See the Finding section for the detailed recommendations.

Management Comments. We provided a draft of this report on October 5, 2007, and management comments were due on November 5, 2007. No management comments were received; therefore, we request that the Under Secretary of Defense for Intelligence and the Director, Defense Security Service comment on this report by February 4, 2008.

Table of Contents

Background

We performed this audit in response to a July 2006 request from the Director, Defense Security Service (DSS). The Director, DSS requested assistance in assessing the effectiveness of the financial management (FM) functions within DSS.

Transition at DSS. Until February 2005, DSS was responsible for performing personnel security investigations (PSIs) for DoD military and civilian personnel as well as for contractor personnel for DoD and 23 other Federal agencies. On January 24, 2003, the Deputy Secretary of Defense and the Director of the Office of Personnel Management (OPM) agreed in principle to transfer the PSI function from DSS to OPM. On October 16, 2004, DoD and OPM finalized that agreement. In February 2005, DSS transferred approximately 1,800 PSI positions and $33.8 million to OPM. As a result, OPM is now responsible for conducting 90 percent of the PSIs in the Federal Government.[1] In September of each year, OPM establishes and publishes the rates it charges all Federal agencies for each type of PSI. However, during FYs 2005 and 2006, OPM charged DoD a surcharge of up to 25 percent on each PSI request, terms agreed to as part of the transfer.

After the transfer, DSS continued to be responsible for the adjudication of security clearances for contractor personnel from DoD and the 23 other Federal agencies.[2] Adjudication is the process of assessing a person's trustworthiness and fitness for a security clearance by reviewing all the information provided during the PSI and granting or denying the requested type of clearance.

Leadership Turnover. Between November 2004 and March 2007, DSS was led by three Acting Directors. The first held the position for 12 months; the second held the position for 6 months and was triple-hatted as the Acting Director, the Chief Operating Officer, and the Chief Information Officer. The third Acting Director was appointed in June 2006 and selected as the permanent DSS Director in March 2007. Among other top positions, prior to July 2006, DSS also did not have a permanent Deputy Director, Chief of Staff, or Chief Information Officer. Since August 2007, the current DSS Director has successfully filled these permanent positions. See Appendix C for a timeline of the changes in key leadership positions at DSS from January 2002 through August 2007.

DSS Mission and Functions After Transfer. DSS is the DoD organization responsible for providing the Secretary of Defense, DoD Components, Federal

[1]The other organizations that conduct PSIs include the Department of State, the Department of Homeland Security, the Federal Bureau of Investigation, and other intelligence community activities.

[2]DSS continues to perform adjudication for confidential, secret, and top secret security clearances for contractor personnel, while the Military Departments, Joint Chiefs of Staff, and Defense Agencies perform adjudication for confidential, secret, and top-secret clearances for DoD military and civilian personnel. The Military Departments, Defense Intelligence Agency, and National Security Agency perform adjudications for DoD military and civilian personnel and contractor personnel requiring clearance levels above top secret.

Government contractors, and 23 other Federal agencies with a full range of security support services. DSS has three components.

- The National Industrial Security Program (NISP) is responsible for overseeing, assisting, and monitoring contractor facilities and contractors that require security clearances to conduct business with DoD as well as with 23 other Federal agencies. NISP oversees approximately 11,000 contractor facilities and their employees that are cleared for access to classified information.

- The Personnel Security Clearance Office[3] encompasses four offices and one program: the Clearance Liaison Office, the Defense Industrial Security Clearance Office, the Polygraph Office, the Counterintelligence Office, and the PSI for Industry Program. In total, the Personnel Security Clearance Office serves as the point of contact within DoD for personnel security operations, polygraph examinations, and counterintelligence support to DoD, and functions as the liaison between DoD and OPM. The PSI for Industry Program centrally identifies, manages, and finances the cost of PSIs for contractors, while the Defense Industrial Security Clearance Office adjudicates security clearances for contractor personnel.

- The Security Education, Training, and Awareness Program provides security education and training to DoD security program professionals and develops security awareness products for their use.

The DSS Director reports to the Under Secretary of Defense for Intelligence, who serves as the senior DoD security official. The Under Secretary of Defense for Intelligence has direct authority, direction, and control over DSS operations.

For FY 2006, DSS was authorized 582 civilian personnel, and spent approximately $345 million in appropriated funds, which included an $80 million congressional reprogramming of funds. The congressional reprogramming allowed DSS to continue operations including processing PSI for Industry requests. For FY 2007, DSS was again authorized 582 civilian personnel and received an appropriation of approximately $324.6 million in operation and maintenance funds. Between April and August 2007, DSS received $32 million in additional funds for the remainder of FY 2007.

Objectives

Our overall audit objective was to determine whether DSS had effective management controls over FM. Specifically, our objective was to evaluate controls over budgeting and managing funds for DSS operations, including payments for PSIs. We evaluated the controls over FM before, during, and after the transfer of the PSI function to OPM. We did not evaluate the costs associated

[3]The Personnel Security Clearance Office, until fall 2006, was known as the Collaborative Adjudication Service.

with the transfer of the PSI function to OPM because DoD Inspector General Report No. D-2007-083, "Transition Expenditures for DoD Personnel Security Investigations for FY 2005," April 10, 2007, addressed the subject. Specifically, that report assessed the DSS controls in place to ensure accuracy of OPM invoices before making payments. See Appendix A for a discussion of the scope and methodology and Appendix B for prior audit coverage related to the objectives.

Review of Internal Controls

We identified a material internal control weakness for DSS as defined by DoD Instruction 5010.40, "Managers' Internal Control (MIC) Program Procedures," January 4, 2006. DSS did not develop an effective system of internal controls over its FM practices to ensure that it:

- complied with Federal and DoD regulations regarding the use of appropriated funds, as well as with appropriation law and regulations; and

- provided personnel with the necessary resources to properly develop, execute, analyze, and monitor the DSS annual budget.

Implementing Recommendation 1. would improve controls over and monitoring of DSS FM functions, requirements, and operations. A copy of the final report will be provided to the senior official responsible for management controls in DSS and in the Office of the Under Secretary of Defense for Intelligence.

Controls Over Financial Management at Defense Security Service

DSS has taken steps to improve FM, but experienced difficulties in managing some aspects of its FM from FYs 2002 through 2007. Specifically, DSS had difficulty estimating the costs of contractor PSI requests, recording and tracking obligations, aging accounts receivable, reviewing unliquidated obligations, and preparing and executing funding documents in compliance with appropriations law and regulations.

The FM difficulties occurred because DSS had not:

- established clearly defined roles and responsibilities for FM,
- developed written policies and procedures for FM,
- provided training to ensure that DSS personnel performing FM functions were knowledgeable of the law and regulations relating to their duties, or
- established a review process to evaluate and monitor controls over FM.

In addition, DSS, until recently, lacked stability in senior management and experienced substantial turnover or vacancies in key FM positions.

As a result, DSS lacked assurance that it would perform its critical mission of processing contractor PSIs. Also, DSS did not record obligations totaling $8.44 million made against 20 MIPRs within the time frame required; did not properly account for $3.2 million in uncollected accounts receivable in the financial statements for FY 2006; and may have incurred potential Antideficiency Act violations totaling approximately $54,000. Without fundamental changes, some already in progress, to DSS FM practices and a more stable management structure, DSS may be hampered in its ability to perform its critical mission.

FM Division

Role. The FM Division of DSS is responsible for budget formulation, budget execution, and accounting to ensure compliance with Federal and DoD law and regulations. Until May 2007, the FM Division was headed by a Comptroller. In May 2007, DSS established and selected a Chief Financial Officer to head FM; however, the FM Division continues to include the Comptroller position.

Structure and Personnel. As of August 2007, the FM Division consisted of the following five branches: Budget Formulation, Budget Execution, Accounting, Performance Improvement, and Audit Readiness. At that time, out of 24 staff positions in the FM Division, 8 were permanent. Of the eight permanent positions, three were vacant: Comptroller, Budget Execution Branch Chief, and Budget Formulation Branch Chief.[4] The remaining 16 positions included 2 augmentees on loan indefinitely from the Defense Finance and Accounting Service, 1 augmentee on loan from the Under Secretary of Defense for Intelligence for a period not to exceed 6 months, and 13 contractors.

From September 2003 to November 2006, DSS had eight Comptrollers, five of whom occupied the position in an acting or temporary capacity. In November 2006, the DSS Director obtained an employee from the Office of the Under Secretary of Defense for Intelligence who had budget and FM experience to function as the Acting Comptroller; that person has since been selected as the DSS Chief Financial Officer.

In addition to the 24 staff in the FM Division, 6 Resource Advisors participated to varying extents in DSS FM activities. Resource Advisors were assigned to each of the three DSS components, as well as to DSS Headquarters, the Office of the Chief Information Officer, and the Counterintelligence Office.

Management of Financial Functions at DSS

DSS experienced difficulties in managing aspects of its financial management functions. Specifically, DSS had difficulty:

- estimating the cost of contractor PSIs; and
- managing financial activities, including recording and tracking obligations, aging accounts receivable, reviewing unliquidated obligations, and preparing and executing funding documents in compliance with regulations and appropriation law.

Estimating the Cost of Contractor PSIs

DSS had difficulty estimating the cost of contractor PSIs for FYs 2003 through 2006. This occurred largely during a period of vacancies and turnover in senior DSS and FM Division positions. DSS did not have a consistent and documented method for estimating contractor PSI caseloads. In addition, DSS did not have a method for estimating costs based on estimates of the caseloads. As a result, in FY 2006, DSS exhausted its budget for contractor PSIs and stopped processing new contractor PSIs for 21 days. Without making fundamental changes in estimating contractor PSI costs, DSS has no assurance that it will be able to perform its critical missions.

DSS was responsible for managing and paying for PSIs for contractor personnel for DoD and 23 other Federal agencies. Contractor PSI costs account for more than 60 percent of the DSS annual budget. The actual costs depended on the

[4]The Budget Formulation Branch Chief and Budget Execution Branch Chief positions have been vacant since September 2006.

number of contractor PSI requests and the costs associated with the type of investigation requested. For FY 2007, for example, a periodic reinvestigation cost $550, while a single-scope background investigation cost $3,550.[5]

Estimation of Caseload. DSS estimated annual contractor PSI caseloads relatively accurately for FYs 2002 through 2006. Table 1 compares estimated and actual caseloads for FY 2002 through FY 2007. As seen in the table, DSS achieved an 88- to 99-percent accuracy rate in estimating caseloads for FYs 2002 through 2006. For FY 2007, however, the preliminary data showed that the accuracy rate declined to 69 percent.

Table 1. Comparison of Estimated and Actual Contractor PSI Caseloads, FYs 2002 Through 2007

Fiscal Year	Estimated Caseload	Actual Caseload	Actual Caseload as a Percent of Estimated Caseload
2002	139,456	138,442	99%
2003	148,998	147,711	99
2004	150,475	132,408	88
2005	145,671	137,944	95
2006	188,068	172,619	92
2007	244,804	168,324*	69

*Annualized caseload based on 35 weeks of actual data through June 2007.

FYs 2002 Through 2007. For FY 2002 through FY 2007, DSS did not have a consistent and documented methodology for estimating PSI caseloads. DSS used surveys of cleared contractor facilities[6] to obtain the expected number and type of PSI requests for the current fiscal year and the next 5 fiscal years (for example, single-scope background investigation or periodic review). Although DSS generally received a 10- to15-percent response rate, DSS officials were unable to explain how DSS used the raw survey data to project the PSI caseload. Further, for FY 2005 and FY 2006, DSS did not use the survey results to estimate caseload; instead, the former Acting Director developed the caseload estimates and did not maintain documentation of those estimates or the methodology used.

FY 2008. In October 2006, the current DSS Director initiated changes to the method for estimating contractor PSI caseloads. In October 2006, the Personnel Security Clearance Office[7] issued a Web-based survey to all of the cleared contractor facilities. DSS asked security officers at those facilities for both the number and type of PSIs needed for the current and the next 5 fiscal years. Approximately 50 percent of cleared contractor facilities responded to the

[5]Periodic reinvestigations are performed to verify that individuals currently holding a clearance should still have access to classified information. Single-scope background investigations are detailed investigations required to obtain a top-secret security clearance and include reviews of an individual's national and local records.

[6]Cleared contractor facilities are eligible to receive awards of classified Government contracts.

[7]In October 2006, DSS transferred the responsibility for estimating the contractor PSI caseload from NISP to the Personnel Security Clearance Office, specifically the Clearance Liaison Office.

revised survey. According to Personnel Security Clearance Office personnel, DSS planned to use the results of the Web-based survey to estimate caseloads starting with FY 2008.

Personnel Security Clearance Office officials considered the initial responses to the Web-based survey promising, but planned to identify additional means to improve the quality of caseload estimates. For example, DSS evaluated the model used by the Department of the Air Force and other methods to estimate the caseloads. In addition to improving the quality of the caseload estimates, DSS officials also wanted to improve the documentation of the methods, assumptions, and data used to develop the caseload estimates. However, as of August 2007, DSS had not fully completed the effort. DSS should continue its efforts to improve the quality and accuracy of caseload estimates and document the method for future use.

Estimation of Costs. DSS experienced difficulties in accurately estimating contractor PSI costs for FYs 2003 through 2006. Table 2 compares the DSS estimated and actual costs for contractor PSIs. The table demonstrates that actual costs ranged from 87 percent to 256 percent of the estimated costs for FYs 2003 through 2006; however, for FYs 2002 and 2007, the cost estimates were relatively accurate.

Table 2. Comparison of Estimated and Actual Contractor PSI Costs, FYs 2002 Through 2007

Fiscal Year	Estimated Cost (millions)	Actual Cost (millions)	Actual Cost as a Percent of Estimated Cost
2002	$ 31.4	$ 30.5	97%
2003	56.5	129.9	230
2004	57.4	146.9	256
2005	117.8	102.2	87
2006	177.5	219.9	135
2007	186.5	187.6*	101

*Annualized cost based on 35 weeks of actual data through June 2007.

DSS did not use the relatively accurate PSI caseload to estimate PSI costs. Consequently, for FY 2003, the actual caseload was 99 percent of the estimated caseload, while the actual cost was 230 percent of the estimated cost. Further, for FY 2006, actual caseload was 92 percent of the estimated caseload, while actual cost was 135 percent of the estimated cost.

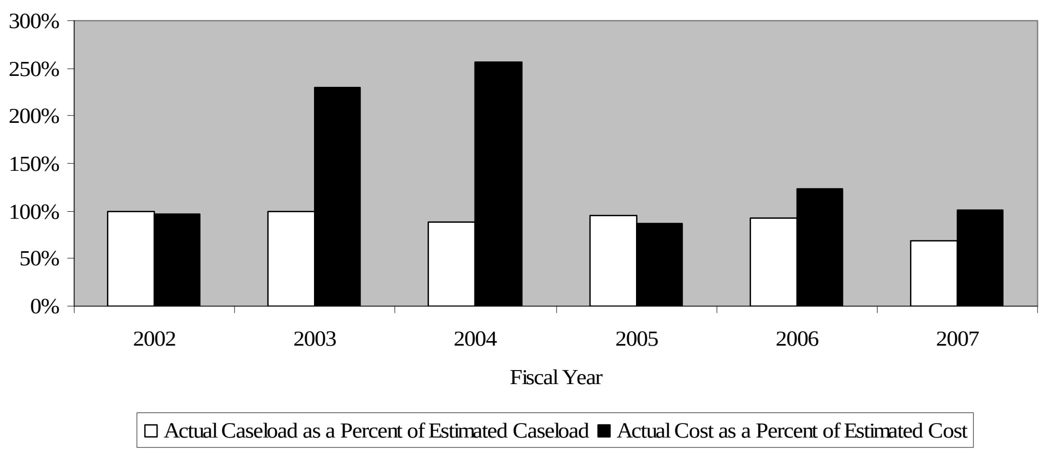
However, as of February 2007, Personnel Security Clearance Office officials stated they were working to ensure that the FY 2008 estimated PSI costs directly correlated with the estimated PSI caseload by establishing a process to multiply the caseload estimates by the estimated OPM rates. Table 3 and the figure accompanying it compare the actual caseload as a percent of the estimated caseload (from Table 1) with the actual cost as a percent of the estimated cost (from Table 2).

Table 3. Comparison of Accuracy of Caseload Estimates and Cost Estimates for Contractor PSIs

Fiscal Year	Actual Caseload as a Percent of Estimated Caseload	Actual Cost as a Percent of Estimated Cost
2002	99%	230%
2004	88	256
2005	95	87
2006	92	135
2007	69*	101

*Annualized caseload based on 35 weeks of actual data through June 2007.

Comparison of Accuracy of Caseload Estimates and Cost Estimates



Method Used in Previous Years To Estimate Costs. DSS did not have a method for estimating contractor PSI costs based on estimated caseloads. NISP and FM Division officials were unable to explain how cost estimates were developed through FY 2006 and were not able to locate any documentation. In addition, no one in NISP, the Personnel Security Clearance Office, or the FM Division could identify a written DSS policy or procedure for translating caseload estimates into cost estimates for budget purposes. The Comptroller attributed the lack of a written policy to the significant turnover in key DSS positions.

NISP officials stated that, for FYs 2004 through 2006, they gave caseload estimates to the DSS FM Division for use in estimating costs. However, we were unable to determine whether the FM Division calculated the cost estimates for FYs 2004 through 2006 using the NISP data because of the turnover in the Comptroller position and the lack of documentation. Officials in the Personnel Security Clearance Office stated that DSS used the estimated caseloads to estimate costs for FYs 2002 through 2004. However, those officials further stated that the former DSS Acting Director did not use the estimated caseloads to estimate costs for FYs 2005 and 2006.

Method Used in FYs 2007 and 2008 To Estimate Costs. To develop the FY 2007 cost estimate, the Personnel Security Clearance Office used the estimated caseload for each type of investigation from the FY 2005 survey and multiplied by the OPM rates for FY 2006 plus 24 percent to account for the OPM surcharge.[8] DSS Personnel Security Clearance Office officials could not explain why the FY 2007 actual caseload was significantly lower than the estimated caseload, but the actual cost roughly equaled the estimated cost, demonstrating that there still was no correlation between the caseload estimate and the cost estimate. In developing the FY 2008 cost estimates, DSS worked to improve the direct correlation between the estimated caseload and estimated cost by establishing a process to multiply the caseload estimates by the estimated OPM rates. It is important for DSS to use accurate caseload estimates for estimating costs because contractor PSIs account for at least 60 percent of the DSS operation and maintenance budget. To improve reliability of the PSI estimates for DSS budgeting purposes, DSS should continue to develop and document a method for estimating costs ensuring a direct correlation between caseload and cost estimates.

Ability To Perform Contractor PSIs. In April 2006, DSS exhausted its budget for contractor PSIs, and the former Acting Director stopped processing new contractor PSIs for 21 days.[9] Without a good methodology to accurately estimate PSI costs, DSS has no assurance that it will be able to perform its critical mission of processing contractor PSIs for the Federal Government. The former Acting Director stated that, because actual costs exceeded estimated costs, she stopped processing new contractor PSIs to avoid exceeding the funds appropriated to DSS; exceeding the funding could result in a violation of the Antideficiency Act. The former Acting Director, the former Comptroller, and Personnel Security Clearance Office officials attributed the higher-than-estimated costs to the surcharge, increased OPM rates, or an unexpected increase in the more expensive types of PSIs. In addition, the former Acting Director stated that DSS lacked sufficient appropriated funds to cover the higher costs because DSS submitted its FY 2006 budget request to Congress before the transfer of the PSI function to OPM.

The former Acting Director believed that DSS needed an additional $188 million to cover the cost of contractor PSIs for the remainder of the FY 2006. However, after the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer requested that Congress reprogram an additional $91 million for DSS, DSS resumed processing PSIs. DSS received an additional $80 million as a result of the Under Secretary of Defense (Comptroller)/Chief Financial Officer request. The $80 million allowed DSS to process contractor PSIs for the rest of FY 2006.

Need for More Accurate Cost Estimates. Before the February 2005 transfer of PSIs to OPM, DSS could accommodate fluctuations in actual costs by adjusting the PSI budget. However, following the transfer, DSS could not make such

[8]As part of the transfer of the PSI function to OPM, OPM could charge DSS up to a 25-percent surcharge in addition to the established OPM fees for each type of PSI requested. During FY 2006, OPM charged a 19-percent surcharge until July 1, 2006, and then lowered the surcharge to 14 percent.

[9]DSS forwarded contractor PSI requests to OPM.

adjustments. Thus, the accuracy of cost estimates became more critical, and inaccuracies affected the ability of DSS to perform its critical missions.

Before OPM Transfer. Before the transfer of PSIs to OPM, DSS managed the costs for PSIs using the DSS Working Capital Fund. Working capital funds come from the sale of supplies and services and are used to pay the costs of providing the supplies or services; fund managers strive to break even over the long term, and they set prices accordingly. The DSS Working Capital Fund was part of the Defense Working Capital Fund. The DSS Working Capital Fund received income from the Military Departments and DoD agencies for PSIs. DSS used the DSS Working Capital Fund to pay for PSIs of DoD military, civilians, and Federal Government contractor personnel. Although working capital funds are designed to break even, when DSS over- or underestimated costs, it made adjustments to the fund in two ways.

- DSS could decrease or increase overall PSI prices. For example, NISP increased FY 2004 prices by a total of $11 million after the actual costs exceeded the estimated costs by $73 million in FY 2003.[10]

- The Under Secretary of Defense (Comptroller)/Chief Financial Officer could transfer funds from the Defense Working Capital Fund to the DSS Working Capital Fund. For example, when the DSS Working Capital Fund closed in September 2006, it had a deficit of approximately $142 million, and the Under Secretary of Defense (Comptroller)/Chief Financial Officer transferred $142 million from the Defense Working Capital Fund to cover the deficit and zero out the DSS Working Capital Fund.[11]

After OPM Transfer. After the February 2005 transfer of the PSI function to OPM, DSS no longer used the DSS Working Capital Fund; however, DSS remained responsible for funding contractor PSIs, whether the PSIs were originated by contractors of DoD or contractors of the other 23 Federal agencies. Without the Working Capital Fund, DSS had to fund the costs with appropriated funds and no longer had the flexibility to handle funding shortfalls. Thus, estimation of costs became critical to DSS budgeting to ensure DSS received sufficient appropriations to cover contractor PSI costs. Unless DSS can accurately estimate the number and types of contractor PSIs, DSS has no assurance that it will be able to fund or perform that mission-critical function.

Congressional Interest in PSI Cost. It is critical that DSS accurately estimate the cost of PSIs for contractors because of added congressional interest. Public Law 109-364, "John Warner National Defense Authorization Act for Fiscal Year 2007," October 17, 2006, directed the Comptroller General to report to Congress on at least the unit cost of a PSI to DoD, the procedures used by DoD to estimate the annual number of PSIs, and any plan developed by DoD to ensure

[10] The adjustments to the FY 2004 rates were across DoD for all military, DoD civilian, and contractor PSIs—not just contractor PSIs.

[11] The DSS Working Capital Fund was no longer used for funding contractor PSIs as of September 2005; however, the fund remained open until September 2006 to accommodate open bills.

adequate funding for PSIs.[12] With the additional congressional interest, it is important that DSS continue to develop and document a method for estimating costs and ensure a direct correlation between the caseload and cost estimates.

Managing Financial Activities

Management of some DSS financial activities needed improvement. Specifically, for FYs 2002 through 2006, DSS did not regularly ensure (1) timely obligation of funds, (2) timely aging of accounts receivable, (3) timely reviews of unliquidated obligations, or (4) proper preparation and execution of Military Interdepartmental Purchase Requests (MIPRs) that affected financial obligations.

Contracting Authority. According to DoD Directive 5105.42, "Defense Security Service," May 13, 1999, DSS can act as its own contracting authority, meaning that DSS may award and administer contracts. However, as of August 2007, DSS did not have a warranted contracting officer on staff, and therefore had to place orders for supplies and services through other DoD and non-DoD agencies. As of August 2007, the DSS Director was working to obtain a warranted contracting officer.

DSS used DD Form 448, "Military Interdepartmental Purchase Request," as the primary means of obligating funding when acquiring supplies or services through other agencies. To determine the adequacy of the process used to prepare, review, obligate, track, and monitor MIPRs, we reviewed a sample of 65 MIPRs (valued at $25 million), dated between September 2002 and February 2006,[13,14] from a universe of 999 MIPRs (valued at $399 million) that were active during FYs 2005 and 2006. We also examined the accounting transactions related to each MIPR to corroborate and supplement the information contained in each MIPR file.

Timely Recording of Obligations. According to DoD Regulation 7000.14-R, "DoD Financial Management Regulation" (FMR), volume 3, chapter 8, section 080301A, "Ten-Day Rule," June 2005:

> [O]bligations shall be recorded in the official accounting records at the time a legal obligation is incurred . . . . In no instance shall obligations be recorded any later than 10 calendar days following the day the obligation is incurred. . . . [O]bligations of $100,000 and more—per . . . accounting line . . . shall be recorded and included in the official accounting records in the same month in which the obligation is incurred.

---

[12] On May 29, 2007, the Comptroller General announced an engagement to address the congressional concerns outlined in Public Law 109-364.

[13] We judgmentally selected 65 MIPRs for review, including MIPRs of large and small values and MIPRs prepared for each of the DSS components. We chose MIPRs against which transactions were recorded in the DSS accounting system as of September 2006.

[14] The current DSS Director has been in place since March 2007 (was acting since June 2006), and the current Acting Comptroller has been in place since November 2006.

Further, according to Defense Federal Acquisition Regulation Supplement PGI 208.7004-2, “Acceptance by Acquiring Department,” September 2001, the activity cannot record an obligation until it receives acceptance of the MIPR, through an acceptance document or a copy of the contract.

Of the 65 MIPRs reviewed, 20 had obligations totaling $8.44 million that DSS did not record within the time frame required by the FMR. The average age of obligations was approximately 73 days, versus the required 10 days, and the longest took 281 days. For example, in April 2005, a $2.7 million obligation for information technology services was not recorded for 69 days, and in December 2004, DSS did not record a $0.7 million obligation for information technology services for 281 days.

Within the DSS Budget Execution Branch, either the Funds Certifier or the FM Analysts were responsible for recording obligations against the MIPR in the accounting system. The 20 obligations were not recorded in the required time frame because the Funds Certifier, a permanent DSS employee, was not aware of the requirement and therefore did not track obligations for timeliness. Furthermore, the FM Division did not have a standard operating procedure for the timely recording of obligations. The Funds Certifier explained that she was not aware of the 10-day rule partially because the on-the-job training she received from a contractor employee did not include the 10-day rule. Because the Funds Certifier was not aware of the 10-day rule, she did not ensure that DSS obtained a copy of the MIPR acceptance or a copy of the contract from the servicing agency in a timely manner. Without the documented acceptance of the MIPR or a copy of the contract, DSS cannot record the obligation. In addition, as of August 2007, the FM Division had no documented policy requiring compliance with the 10-day rule.

When DSS did not timely record the obligations totaling $8.44 million, the DSS accounting records incorrectly showed those funds as available for use. This oversight increased the risk that DSS could violate the Antideficiency Act by obligating more funds than were available in its appropriation. Therefore, it is important that DSS expedite issuing policy to address timely recording and tracking of obligations. In addition, it would be beneficial to provide training to those obligating funds to ensure that obligations are recorded in accordance with the 10-day rule. DSS should perform periodic monitoring to ensure that the FM Division completes aging of accounts receivable before the end of each fiscal year.

Timely Aging of Accounts Receivable. The FMR, volume 4, chapter 3, “Receivables,” July 2006 ,[15] requires that delinquent (unpaid after the due date) receivables are to be aged starting 1 day after the payment due date, that expenditures incurred for completed performance are to be promptly recorded as billed receivables, and that the performing entity should ensure the billed receivables are promptly charged and collected. The purpose of the FMR requirement is to promptly record monies due an organization; to collect overdue

[15] This chapter was updated in July 2006, but the requirement did not change from the December 2001 version; therefore, the requirement applied throughout FY 2006.

funds; and to make those funds available for other purposes by the receiving organization, in this case DSS.

According to DSS FM Accounting Branch personnel, they were responsible for monitoring accounts receivable for items such as tuition costs for the Security Education, Training, and Awareness Program and for providing classified internal services within DoD. For the entire FY 2006, the Accounting Branch did not timely record accounts receivable and did not conduct any aging of accounts receivable. As a result, DSS reported in its FY 2006 annual financial statements a total of $3.2 million in uncollected accounts receivable.

Of the uncollected amounts totaling $3.2 million, the Accounting Branch took 102 days to record in the DSS accounting system an account receivable for $0.2 million. Another account receivable for $0.2 million took the Accounting Branch 121 days to record, and as of April 2007, DSS had not collected the funds. According to FM Division personnel, the recording, aging, and collecting of accounts receivable did not occur because it was unclear who was responsible. According to FM Division personnel, both staff members assigned to the Accounting Branch were temporary augmentees from the Defense Finance and Accounting Service who were tasked to perform specific assignments, and aging accounts receivable was not among their assigned tasks. Furthermore, the FM Division did not have a documented procedure for performing this function.

In April 2007, FM personnel identified a need for written policy and procedures on aging accounts receivable; however, as of August 2007, they had not been drafted. As of November 2006, Accounting Branch personnel had initiated monthly aging of accounts receivable within the Accounting Branch to ensure accounts receivable were both billed and collected timely in FY 2007. It is commendable that DSS has recognized the need for formal policy on timely aging of accounts receivable. To better formalize the process, DSS should issue policy on aging accounts receivable, delegate the responsibility in writing, and perform quality assurance in the form of periodic monitoring to ensure that the FM Division completes aging of accounts receivable before the end of each fiscal year.

Timely Reviews of Unliquidated Obligations. The FMR, volume 3, chapter 8, section 0804, "Triannual Reviews of Commitments and Obligations," June 2005, requires DoD agencies to perform reviews of unliquidated obligations[16] and commitments three times each year. The FMR also requires fund holders, with assistance from supporting accounting offices, to review commitment and obligation transactions "for timeliness, accuracy, and completeness during each of the 4-month periods ending on January 31, May 31, and September 30 of each fiscal year." The FMR, volume 3, chapter 8, section 080403, "Responsibilities of Fund Holders," June 2005, requires triannual reviews be completed "no later than 14 days following the end of January and of May, as well as by September 30 of each fiscal year." Furthermore, the FMR states that triannual reviews should be conducted on direct appropriations, reimbursable transactions, and revolving and trust funds. The purpose of the triannual reviews is to ensure unliquidated

[16]Unliquidated obligations are the funds associated with an obligation that have not been spent or are still outstanding.

obligations are recorded and are in the proper stage of accounting—committed, obligated, or expensed—and to determine whether the amounts are valid and correct.

From September 2005[17] through May 2007, DSS FM Division either did not complete or did not timely complete triannual reviews of outstanding obligations. From September 2005 through May 2007, DSS was required to complete six triannual reviews, but completed only three reviews, of which only two were done within the required time frame of 14 days. Table 4 identifies the review periods, review due dates, and actual dates associated with the past six triannual reviews.

Table 4. DSS Completion of Triannual Reviews

Review Period End	Review Due Date	Actual Date of Review (Days Late)
September 30, 2005	September 30, 2005	Not Completed
January 31, 2006	February 14, 2006	March 17, 2006 (31 days)
May 31, 2006	June 14, 2006	Not Completed
September 30, 2006	September 30, 2006	August 31, 2006 (0 days)
January 31, 2007	February 14, 2007	Not Completed
May 31, 2007	June 14, 2007	May 24, 2007 (0 days)

In September 2005, the FM Division assigned responsibility for performing the triannual reviews to the Resource Advisors and the Budget Execution Branch. However, FM Division personnel were unable to explain why past reviews were not completed. In addition, at least one of the Resource Advisors stated that he had other duties that took precedence over completing the triannual reviews. The Acting Director was successful in publishing the Triannual Review policy in January 2007. However, according to Accounting Branch personnel, DSS did not complete the January 2007 triannual review because a majority of the Resource Advisors did not provide their results in a timely fashion to the FM Division. The Resource Advisors and the FM Analysts successfully used the Triannual Review policy to complete the May 2007 triannual review on time. In the past, according to Accounting Branch personnel, no one within the FM Division monitored the completion of triannual reviews because of the turnover in the Comptroller position and vacant Budget Execution Chief position.

By not completing the triannual reviews, DSS did not identify funds that could be deobligated and used for other purposes. For example, when DSS completed the January 31, 2006, and September 30, 2006, reviews, approximately $211,000 and $275,000, respectively, were deobligated, making those funds available for other uses before the funds expired. It is commendable that DSS initiated formalizing

[17]The requirement to complete the triannual review was initiated by the Under Secretary of Defense (Comptroller)/Chief Financial Officer in June 2005, with the first full triannual review due at the end of FY 2005.

policy on conducting triannual reviews. As DSS continues to implement the January 2007 triannual review policy, the Resource Advisors and FM Analysts will be able to complete triannual reviews in a timely manner. DSS should continue to perform quality assurance in the form of periodic monitoring to ensure that the triannual reviews are completed on time.

Proper Preparation and Execution of MIPRs. From FYs 2002 through 2006, the FM Division did not consistently prepare and approve MIPRs in compliance with the law and regulations that govern the use of Federal appropriations. Specifically, DSS did not comply with the bona fide needs rule and potentially violated the Antideficiency Act. Also, many of the MIPRs that we reviewed had unclear descriptions of the supplies and services required and unclear periods of performance.

MIPR Process. Once a DSS component identified the need for a supply or service, the component's Resource Advisor prepared and submitted a MIPR to the FM Budget Execution Branch. Within the Budget Execution Branch, an FM Analyst (a contractor employee) reviewed each MIPR for completeness and accuracy and determined whether sufficient funds were available to procure the supply or service. Then the Funds Certifier (a Government employee) reviewed the MIPR and certified that funds were available. After certification, the MIPR was returned to the Resource Advisor, who then forwarded the MIPR to the Federal agency that would contract for the supplies or services. The requesting component's Resource Advisor, or another designated person within that component, was responsible for monitoring the MIPR to ensure that the component received the requested supplies or services.

Compliance With Appropriation Law and regulations. Of the 65 MIPRs reviewed, 2 may not have complied with the Antideficiency Act. The potential violations occurred when DSS did not meet the bona fide needs rule. The Antideficiency Act is codified in several sections of United States Code, such as in section 1341(a), title 31 [31 U.S.C. 1341(a)], and is one of the major laws through which Congress exercises its constitutional control of the public purse. Violations of other laws may create violations of the Antideficiency Act provisions, including the bona fide needs rule. The bona fide needs rule, codified in 31 U.S.C. 1502(a), states that appropriations are available for designated periods of time and, when using those funds, an organization must have a bona fide need for the requirement in the year(s) that the appropriations are available for obligation. However, if an agency purchases the supplies or services in the year the appropriations are allowed but schedules delivery of those supplies or services for a fiscal year beginning after the appropriation has expired, the agency may not be complying with the bona fide needs rule, potentially leading to a violation of the Antideficiency Act. The FMR, volume 2A, chapter 1, "General Information," June 2004, states that operation and maintenance appropriations are available for obligation for 1 year.

The two instances discovered in reviewing the 65 MIPRs are as follows.

- The Headquarters Resource Advisor issued MIPR NMIPR05970390, dated September 27, 2005, to the Army Contracting Agency for $15,948 in FY 2005 operation and maintenance funds for "providing a training class that would be scheduled at a later date." On September 28, 2005, the Army Contracting Agency awarded a contract to Northrop Grumman for $15,948 to provide the training in December 2005. This action did not comply with the bona fide needs rule for two reasons. First, DSS had not clearly defined the requirement and had no reasonable expectation of receiving the training in FY 2005. Second, the operation and maintenance appropriations used to fund the contract expired on September 30, 2005, while the training (the service being received) was not scheduled to take place until December 2005.

- The Chief Information Officer's Resource Advisor issued MIPR NMIPR05970371 on August 26, 2005, to the Defense Information Technology Contracting Organization for $38,167 of FY 2005 operation and maintenance funds for hardware maintenance from August 1, 2005, through March 31, 2007. The Defense Information Technology Contracting Organization took the following contract actions to fulfill the requirements:

  — issued Contract DCA200-02-A-5011 on September 30, 2005, for $16,051 for hardware maintenance to be provided from October 1, 2005, through September 30, 2006; and

  — issued Contract Modification DCA200-02-A-5011/0053 on September 30, 2006, for $12,652 for hardware maintenance to be provided from October 1, 2006, through September 30, 2007.

  These actions did not comply with the bona fide needs rule because both the contract and the contract modification were awarded using operation and maintenance appropriations from the current year for work to be performed in the following years. Specifically, DSS used funds that were not available after September 30, 2005, to fund activities for FY 2006 and FY 2007.

Neither the Resource Advisors nor the FM Analysts were aware that these contracting actions violated the bona fide needs rule. Specifically, the Chief Information Officer's Resource Advisor stated that he believed he had properly used FY 2005 operation and maintenance funds. According to the FM Analyst, senior management directed that the MIPR be processed with the FY 2005 operation and maintenance funds if the servicing activity would accept the MIPR. The improper application of the bona fide needs rule could constitute a violation of the Antideficiency Act. According to FMR, volume 14, chapter 3, "Preliminary Reviews of Potential Violations," April 2003, it is the responsibility of the agency to investigate potential Antideficiency Act violations once it learns of them.

Clarity of Descriptions of Supplies and Services. The FMR, volume 11A, chapter 3, "Economy Act Orders," April 2000, requires that MIPRs specifically, definitely, and certainly describe the supplies and services requested. MIPR descriptions should be specific enough to ensure that the appropriate funds are being used, that any amendments are within the scope of the work to be performed, and that confirmation can be made that the supplies and services were received and were adequate. However, for 17 of the 65 MIPRs reviewed, valued at $12.4 million, Resource Advisors did not provide sufficient details describing the supplies or services requested. In one case, the Headquarters Resource Advisor forwarded a $0.3 million MIPR to the Budget Execution Branch with a description of "FM, HR [Human Resources], CO [Chief of Operations], SC [security coordination], SS [Support Services] support funding." In another case, the Chief Information Officer's Resource Advisor prepared a $4.75 million MIPR that described the services required simply as "JPAS [Joint Personnel Adjudication System] Support."

In general, the Resource Advisors did not provide additional supporting documentation to the Budget Execution Branch to clarify MIPR requirements. Budget Execution Branch personnel, including the FM Analyst (contractor) and the Funds Certifier (government employee) approved the MIPRs. The Resource Advisors did not provide additional details in the MIPR descriptions because they stated they had received no guidance or training to indicate that the descriptions were insufficient. In turn, Budget Execution Branch personnel did not return the MIPRs for having incomplete information. During interviews, a Budget Execution Branch staff member stated that he did not question the MIPRs or return them to the Resource Advisors for clarification because no one instructed him to flag or return MIPRs with unclear or vague descriptions. Because the descriptions on the MIPRs could encompass a wide variety of supplies and services, it is difficult to determine whether DSS used the correct appropriated funds or whether DSS received the correct supplies or services. Thus, clarification of what constitutes proper preparation of a MIPR and training in MIPR preparation could prevent this in the future. In February 2007, the DSS Acting Comptroller identified the need for policies and procedures on the preparation and processing of MIPRs.

Clarity of Statements of Period of Performance. Defense Federal Acquisition Regulation Supplement PGI 253_208, "Required Sources of Supplies and Services," September 2001, requires that the requesting agency clearly state the period of performance on each MIPR. However, DSS did not define the period of performance for 11 of the 65 MIPRs reviewed, totaling approximately $8.4 million. For example, FM personnel issued a MIPR dated September 2003 and valued at $0.3 million to the U.S. Army Personnel Command for the "temporary use of Army Reserve soldiers." However, the MIPR did not specify any period of performance. In another case, the DSS, Chief Information Officer's personnel prepared a MIPR dated April 2005 for approximately $1 million and then issued an amendment to the MIPR, dated September 2005, for approximately $0.4 million, indicating a period of performance on the amendment that overlapped with the period of performance on the MIPR. During interviews, the Resource Advisors said that they considered the periods of performance to be acceptable because the Budget Execution Branch never returned the MIPRs for being incomplete or unclear. Further, the Resource Advisors stated that they had not received any guidance or training on the level of detail required on a MIPR until October 2006.[18] Further, the FM Analysts stated that they did not question the unclear periods of performance on the MIPRs because they did not have a clear understanding of what constitutes a comprehensive period of performance.

By not clearly defining the period of performance, DSS did not comply with the Defense Federal Acquisition Regulation Supplement and created difficulty for the supplying agency to ensure it met the requirements of the MIPR. In addition, DSS could have violated the Antidefiency Act if the period of performance was not consistent with the period allowed for the type of funds used.

DSS should initiate reviews to determine whether the improper use of Government funds related to MIPRs NMIPR05970390 and NMIPR05970371 resulted in violations of the Antideficiency Act or of other regulations governing the use of appropriated funds. In addition, DSS needs to develop and implement policies and procedures that specifically define an acceptable description of supplies and services and a clear period of performance. Furthermore, the DSS Director needs to train the Resource Advisors, the FM Analysts, and the Funds Certifier on the proper preparation and review of MIPRs, as well as on the proper use of appropriated funds. Finally, DSS should also perform quality assurance in the form of periodic monitoring to ensure MIPRs are prepared and executed properly.

DSS System of Controls for FM

DSS recognized the need to better define roles and responsibilities, establish written policies and procedures, and provide training. In 2005 the organization developed a review process to evaluate corporate internal controls over financial reporting. However, the process was not fully implemented because of a lack of continuity in senior management and vacancies in key FM Division positions. For the same reasons, a process to ensure compliance with internal controls and implementation of corrective actions identified during the reviews was not fully implemented.

Guidance on Management Controls. Management controls provide a valuable tool to organizations to ensure that processes are working as intended and in compliance with law and regulations. According to Office of Management and Budget Circular No. A-123, "Management Accountability and Control," June 21, 1995, management controls are:

> . . . the organization, policies, and procedures used to reasonably ensure that (i) programs achieve their intended results; (ii) resources are used consistent with agency mission; (iii) programs and resources are protected from waste, fraud, and mismanagement; (iv) laws and

[18] In October 2006, the lead FM Analyst sent an e-mail on behalf of the former Comptroller to Budget Execution Branch personnel and the Resource Advisors providing guidance on what the FM Division considered a clear period of performance.

regulations are followed; and (v) reliable and timely information is obtained, maintained, reported and used for decision making.

DSS Assessments of FM Internal Controls. Office of Management and Budget Circular A-123 requires Federal agencies to develop, implement, and document effective internal controls and annually assess and report on the effectiveness of internal controls. In FY 2005, in accordance with Office of Management and Budget Circular A-123, DSS defined a process and methodology to assess, document, and report on the effectiveness of the internal controls over FM functions. In FY 2006, DSS began formal assessments of FM internal controls. The DSS assessments identified internal control weaknesses in processing and recording cash receipts and disbursements, recording accounts receivable and accounts payable, and anticipating payments of Federal employee compensation taxes. To address these weaknesses, DSS developed and approved corrective actions. The corrective actions included documenting and implementing policies and procedures, training FM Division and other DSS personnel, implementing electronic document storage, and communicating roles and responsibilities to DSS staff. In addition to the corrective actions developed by DSS, in December 2006, shortly after starting, the Acting Comptroller established a Resource Management Process to serve as a foundation for all future policies, training, and restructuring regarding the FM processes at DSS. Specifically the Resource Management Process defined overall FM responsibilities throughout DSS, defined the knowledge that Resource Advisors should possess, and established two corporate boards to make overall financial decisions. Furthermore, in its FY 2007 Annual Statement required under the Federal Managers' Financial Integrity Act of 1982,[19] dated August 20, 2007, DSS identified and reported internal control weaknesses and corrective actions associated with processing and recording accounts payable and accounts receivable.

In spite of identifying internal control weaknesses and planning corrective actions, DSS was slowed in the implementation of the corrective actions by a lack of continuity in senior management and vacancies in key FM Division positions (since September 2006). In addition, DSS did not have a quality assurance process to monitor implementation of corrective actions.

Continuity in DSS Management. DSS has been unable to fully implement all the corrective actions, particularly since the transfer of the PSI function to OPM, because of the lack of continuity in senior management since 2002. With five Directors (three acting) within the last 5 years, at least nine Comptrollers (six acting) during the same period, including five Comptrollers during the transfer of the PSI function to OPM, DSS management functioned largely in a reactive mode. In addition, when DSS stopped processing contractor PSIs in April 2006, the former Acting Director stated she was also functioning as the Chief Information Officer and the Chief Operating Officer. The current Director stated that she spent the first 6 months of her tenure putting out fires. Further, the last two Comptrollers, one of whom was acting, stated that they spent much of their time solving near-term financial problems. The most

[19] The Annual Statement required under the Federal Managers' Financial Integrity Act of 1982 is the reporting requirement outlined in Office of Management and Budget Circular A-123.

recent Acting Comptroller also stated that being a part-time comptroller obviously limited his ability to oversee FM functions. In May 2007, the DSS Director selected the Acting Comptroller as the Chief Financial Officer and announced plans to retain the Comptroller position, but as of August 2007 still needed to hire a Comptroller.

Continuity in Other Key Positions. In addition to turnover in the Director and Comptroller positions, the vacancies in key positions within the FM Division limited the DSS Comptrollers' (permanent and acting) ability to implement corrective actions. The vacant positions within the FM Division included those of the Budget Execution and Budget Formulation Branch Chiefs, which have both been vacant since September 2006. The vacancies in those two key FM positions further reduced the time the various Comptrollers could spend on ensuring implementation of corrective actions because the Comptrollers had to oversee the day-to-day operations of both the Budget Formulation and Budget Execution branches in addition to their own work. To better provide oversight of both Government and contractor personnel, DSS should expedite filling both the Budget Execution and Budget Formulation Branch Chief positions.

Process for Monitoring Implementation of Corrective Action Plans. Finally, DSS was slowed in implementing corrective action plans because it does not have a process in place to ensure regular monitoring of corrective action plans. For example, in developing the corrective action plan, DSS identified approximately 19 policies and procedures that needed to be developed; however, as of August 2007, only 5 of those policies and procedures had been issued. The remaining 14 policies and procedures were either in draft or had not yet been started. Among the policies and procedures being developed was the DSS Resource Management Handbook, which will provide DSS personnel with a comprehensive guide on the DoD and DSS budget development and execution processes. See Appendix D for a listing of the 19 policies and procedures and the stage of development. According to the Acting Comptroller and Accounting Branch personnel, the policies and procedures are in various stages of development because of lack of personnel to both develop and monitor the development of the policies. DSS can benefit from a dedicated staff to periodically monitor and assess the implementation of the policies, procedures, and corrective action plans.

Implementation of Corrective Actions

DSS management understands the value of effective internal controls and is using the financial reporting reviews required by the Office of Management and Budget Circular A-123 to identify corrective actions needed. DSS has taken proactive steps, including establishing a process to review internal controls for FM functions, identifying needed policies and procedures, defining roles and responsibilities, and identifying other needed corrective actions. In addition, DSS management has filled many key leadership positions. However, DSS still needs to ensure the corrective actions are successfully implemented. Implementation of corrective actions should facilitate preparation of sound budget estimates and requests and, therefore, help ensure that DSS has the resources to perform its critical missions.

The Under Secretary of Defense for Intelligence has oversight responsibilities for DSS and was involved in the transfer of the PSI function from DSS to OPM. To preclude future budgetary and financial management problems, the Under Secretary of Defense for Intelligence should actively assist and provide oversight of DSS to ensure that DSS continues to pay for PSIs, not only for DoD, but also for 23 other Federal agencies.

Organizational Review of DSS

In July 2006, the DSS Director requested the Air Force's 4th Manpower Requirements Squadron to conduct an organizational review of DSS - in particular, to evaluate the proper functional alignment and necessary staffing levels of five DSS offices.[20] The Air Force report, dated March 2007, included the FM Division and included issues similar to those found during this audit. The Air Force report stated the following.

- The FM Division did not have standard operating procedures in the Budget Execution Branch.
- FM Division employees were concerned about not having the necessary skills to deliver quality products in a timely manner.
- FM Division employees expressed the need for training to better equip themselves to accomplish their FM functions.
- The FM Division was not adequately staffed to establish and maintain a quality assurance program or to conduct cost analysis functions.
- The majority of tasks in the Budget Formulation and Budget Execution Branches were performed by contractors, who could not obligate Government funds. This limitation created bottlenecks as documents requiring approval were routed through a single point of contact for approval. As such, job requirements were not being performed. Not performing required tasks put DSS at risk of violating DoD and Federal regulations or improperly appropriating funds.

The recommendations in the Air Force report included that DSS add, in total, seven positions to the FM Division, fill the vacant Branch Chief positions, and establish and institutionalize policies and procedures throughout the organization. The Air Force report also stated that policies and procedures could reduce work effort and improve credibility, data comparability, and legal defensibility. Finally, the report stated that the FM Division should develop a training program

[20]The five DSS offices were the Clearance Liaison Office, Financial Management Office, Human Resources Office, Office of Chief Information Officer, and Support Services Office.

on management controls, accounting, auditing, and governmental budgeting and that the Comptroller should add a Training Manager to the FM Division staff.

Recommendations

1. We recommend that the Director, Defense Security Service:

a. Develop and document a reliable methodology for estimating the number of contractors needing personnel security investigations and the cost of those investigations.

b. Initiate preliminary reviews, in accordance with DoD Regulation 7000.14-R, "Financial Management Regulation," to determine whether the improper use of Government funds for Military Interagency Purchase Requests NMIPR05970390 and NMIPR05970371 resulted in Antideficiency Act violations or other funding violations.

c. Develop and implement written policies and procedures for efficient and effective financial management. The written policies and procedures should, at a minimum:

(1) Delegate the responsibility for recording obligations to at least one person and a backup, define the process for timely recording obligations, and establish periodic monitoring of obligations to ensure the Financial Management Regulation requirement for recording obligations is met.

(2) Delegate the responsibility for aging accounts receivable to at least one person and a backup, define the process for aging accounts receivable, and establish periodic monitoring of accounts receivable to ensure they are aged timely.

(3) Define what constitutes an acceptable description of supplies and services and a clear period of performance for Military Interagency Purchase Requests, and define the process for rectifying errors on Military Interagency Purchase Requests.

(4) Define the appropriate use of current and expired funds to comply with Federal appropriations law and regulations.

d. Establish training requirements for Defense Security Service staff involved in the preparation and review of Military Interagency Purchase Requests so that the requests contain complete and accurate descriptions of supplies and services and well-defined periods of performance. The training should cover the proper use of appropriated funds, emphasizing the laws governing the bona fide needs rule and the Antideficiency Act.

e. Establish a dedicated responsibility for performing quality assurance reviews that evaluate implementation and success of corrective actions by the Defense Security Service to improve financial management functions.

f. Fill the Comptroller, Budget Formulation Branch Chief, and Budget Execution Branch Chief positions.

2. We recommend that the Under Secretary of Defense for Intelligence assist with and exercise oversight of the Defense Security Service financial management function, including budget formulation and budget execution.

Management Comments Required

The Office of the Under Secretary of Defense for Intelligence and the Director, Defense Security Service did not comment on a draft of this report. We request that both provide comments on the final report by February 4, 2008.

Appendix A. Scope and Methodology

We conducted this performance audit from July 2006 through October 2007 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We performed this audit to evaluate whether DSS had effective management controls over its FM function. Specifically, we evaluated the DSS controls over the development of the estimates for contractor PSI requirements and the agency's annual budget, the identification of mission-essential requirements, and the execution of appropriated funds. We also evaluated management controls over the preparation, approval, and completeness of documents used to commit and obligate appropriated funds. We performed this audit at DSS headquarters and at two DSS field offices: the Security Education, Training, and Awareness Program in Linthicum, Maryland, and the Defense Industrial Security Clearance Office in Columbus, Ohio. We reviewed documents related to budget formulation, contracting, and budget execution, as well as Federal and DoD policies, procedures, guidance, and statutory requirements related to budget development, budget execution, and fiscal law. In addition, we reviewed DSS staff's position descriptions, the United States Air Force 4th Manpower Requirements Squadron's "Organizational Review of DSS," and other documentation related to staffing. Further, we interviewed current and former DSS employees, including agency Directors, Comptrollers, FM personnel, Resource Advisors, augmentees, and contractors. We also interviewed personnel from the Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer, the Office of the Under Secretary of Defense for Intelligence, the Office of the Deputy Chief of Staff of the Army for Intelligence, the Naval Criminal Investigative Service, and the Air Force Consolidated Adjudication Facility.

To determine the adequacy of the process that DSS used to prepare, review, obligate, track, and monitor MIPRs, we selected a judgmental sample of 65 MIPRs out of 999 MIPRs issued between September 2002 and February 2006 with transactions in the accounting system between October 1, 2005, and September 6, 2006. The 65 MIPRs reviewed were valued at $25 million out of a universe of transactions worth $399 million. Our judgmental sample included MIPRs of large and small values, and MIPRs prepared in each of the DSS components. We reviewed several aspects of each MIPR, including whether a determination and finding document was prepared, when required; whether the delivery requirements were stated clearly; whether the required supplies or services were described adequately; and whether obligations were recorded in a timely manner. We also assessed whether the funding was used in accordance with appropriations law and regulations.

Use of Computer-Processed Data. We used computer-processed data, including data from the accounting transaction database provided by DSS. We did not perform a formal reliability assessment of the computer-processed data. However, we compared the data with supporting documentation to verify that data from the database were accurate.

Use of Technical Assistance. We obtained technical assistance from the DoD Office of the Inspector General, Office of General Counsel to ensure accurate interpretation and application of several appropriation and contracting laws and regulations. Specifically, the Office of General Counsel provided legal advice on the determination of potential violations of the Antideficiency Act and compliance with the FMR.

Government Accountability Office High-Risk Area. The Government Accountability Office (GAO) has identified several high-risk areas in DoD. This report provides coverage of three high-risk areas: DoD Financial Management, DoD Contract Management, and DoD Personnel Security Clearance Program.

Appendix B. Prior Coverage

During the last 5 years, the GAO and the DoD IG have issued eight reports discussing DSS FM and the DoD personnel security clearance program. 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.mil/audit/reports.

GAO

GAO Report No. GAO-06-748T, "New Concerns Slow Processing of Clearances for Industry Personnel," May 17, 2006

GAO Report No. GAO-06-747T, "DoD Personnel Clearances: Funding Challenges and Other Impediments Slow Clearances for Industry Personnel," May 17, 2006

GAO Report No. GAO-05-842T, "Some Progress Has Been Made but Hurdles Remain to Overcome the Challenges that Led to GAO's High-Risk Designation," June 28, 2005

GAO Report No. GAO-05-207, "High-Risk Series," January 2005

DoD IG

DoD IG Report No. D-2007-083, "Transition Expenditures for DoD Personnel Security Investigations for FY 2005," April 10, 2007

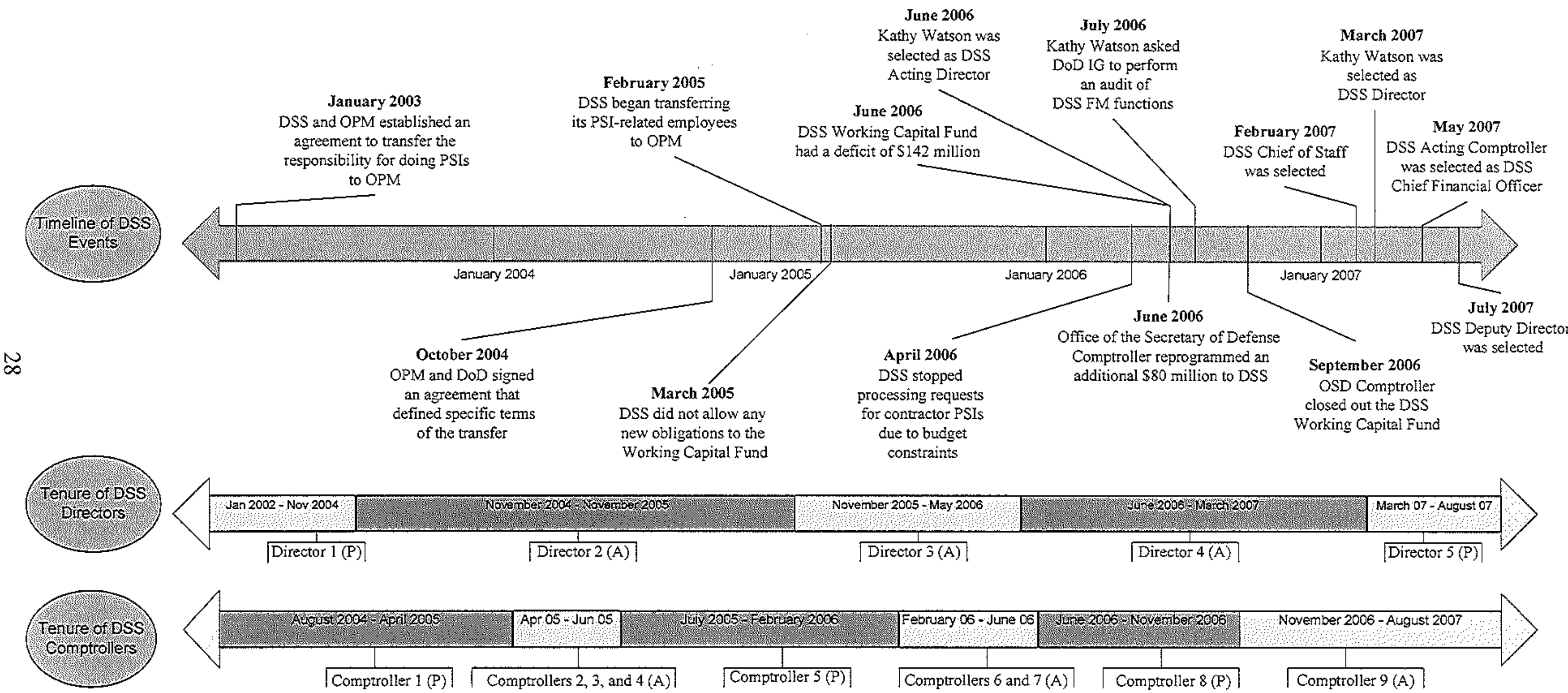
DoD IG Report No. D-2007-042, "Potential Antideficiency Act Violations on DoD Purchases Made Through Non-DoD Agencies," January 2, 2007

DoD IG Report No. D-2007-023, "FY 2005 DoD Purchases Made Through the National Aeronautics and Space Administration," November 13, 2006

DoD IG Report No. D-2003-112, "Contracting Practices of the Defense Security Service for Personnel Security Investigations," June 27, 2003 (For Official Use Only)

Appendix C. Timeline of Events and Key Personnel

Below is a timeline of the events and personnel that had a major effect on the decisions about how to conduct business at DSS. Specifically, the timeline outlines the major events from January 2002 through August 2007 that affected DSS, as well as the changes in DSS overall leadership and FM Division leadership.



KEY FOR TIMELINE: 2002-Present
P - Permanent A - Acting

Appendix D. Status of DSS Policies and Procedures for FM Functions

As of August 2007, under the direction of the current DSS Director and Acting Comptroller (who, as of May 2007, became the Chief Financial Officer), DSS identified approximately 19 different policies and procedures to be developed or updated to improve the internal controls in the FM Division. The 19 policies and procedures were in various stages of development: 5 had been issued; 7 were in draft format; and the remaining 7 had yet to be started. Below is a detailed listing of the 19 policies and procedures by stages.

- DSS developed and issued five policies and procedures addressing the following:

  — Triannual Reviews, dated January 12, 2007;
  — Problem Disbursements, dated January 19, 2007;
  — Federal Employees Compensation, dated April 13, 2007;
  — Civilian Pay, dated June 22, 2007; and
  — PSI Billing Process, dated August 1, 2007.

- DSS had seven policies and procedures in draft format addressing the following:

  — Government Purchase Card,
  — Resource Management Handbook,
  — Commitment and Obligations,
  — Accrued Unfunded Leave Liability,
  — Accounting for Leases,
  — Plant, Property, and Equipment, and
  — Budget Execution.

- DSS had identified seven policies and procedures for development, but had not started developing them. They will address the following:

  — Accounts Receivable,
  — Audited Financial Statements,
  — Defense Travel System and Permanent Change of Station Travel Policy,
  — Intra-government Procedures,
  — Maintenance and Disposition of Records,
  — MIPR Processing, and
  — Processing SF 1080.

Appendix E. Report Distribution

Office of the Secretary of Defense

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

Department of the Navy

Naval Inspector General
Auditor General, Department of the Navy

Department of the Air Force

Auditor General, Department of the Air Force

Combatant Command

Inspector General, U.S. Joint Forces Command

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 Homeland Security and Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Oversight and Government Reform
House Subcommittee on Government Management, Organization, and Procurement,
    Committee on Oversight and Government Reform
House Subcommittee on National Security and Foreign Affairs,
    Committee on Oversight and Government Reform

Team Members

The Department of Defense Office of the Deputy Inspector General for Auditing, Readiness and Operations Support prepared this report. Personnel of the Department of Defense Office of Inspector General who contributed to the report are listed below.

Wanda A. Scott
Kimberley A. Caprio
Rhonda L. Ragsdale
Patrice L. Berry
Robert P. Goldberg
Patrick M. Sampson
Cynthia G. Williams
Maurice L. Foster
Tabitha J. Lemley
Burrell C. Leary
Wilvia Espinoza
Sharon D. Walker
Patricia A. Papas
Allison E. Tarmann


Inspector General
Department of Defense