



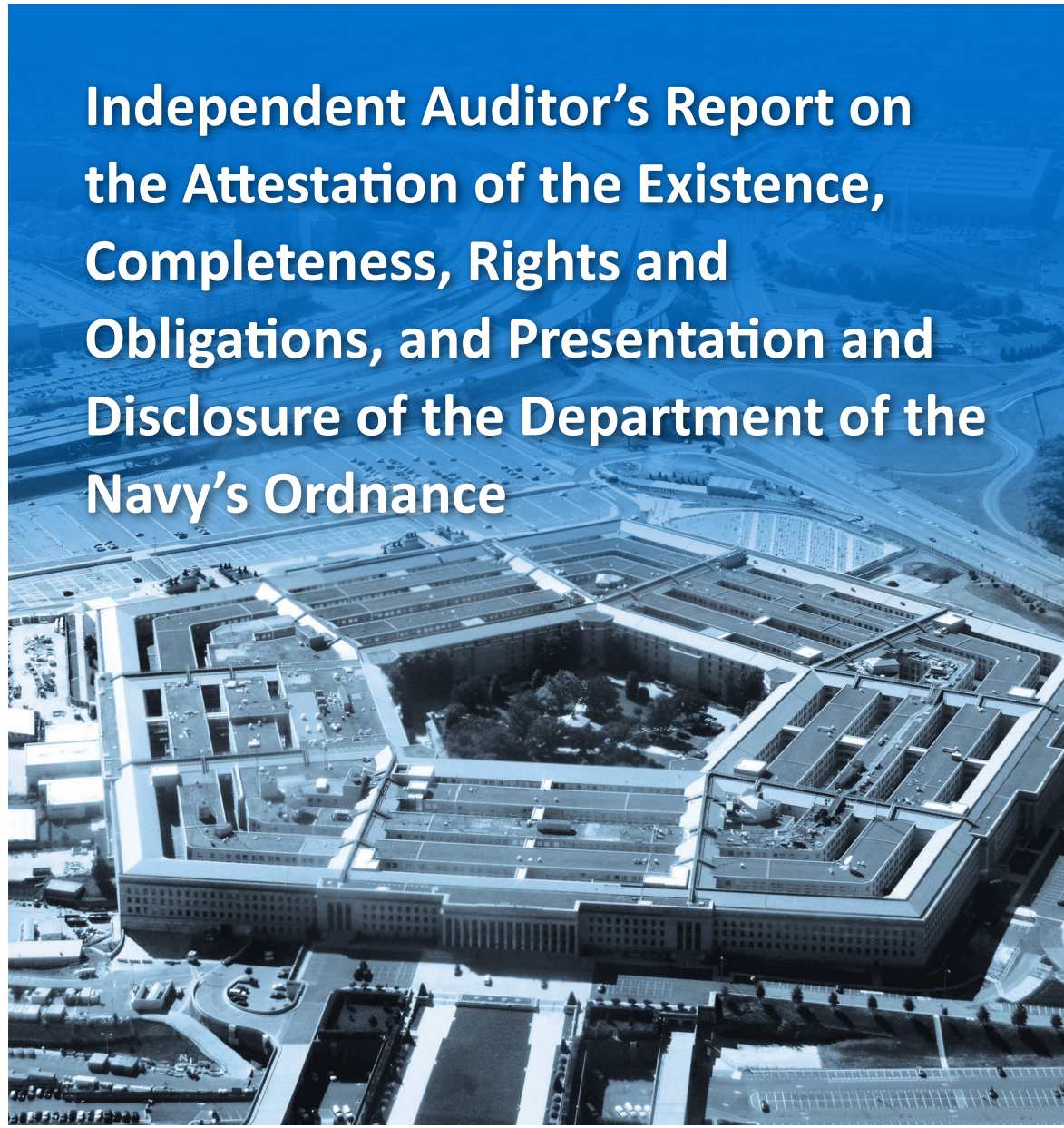
INSPECTOR GENERAL

U.S. Department of Defense

MARCH 25, 2014



Independent Auditor's Report on the Attestation of the Existence, Completeness, Rights and Obligations, and Presentation and Disclosure of the Department of the Navy's Ordnance



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**INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
4800 MARK CENTER DRIVE
ALEXANDRIA, VIRGINIA 22350-1500**

March 25, 2014

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)/
CHIEF FINANCIAL OFFICER, DOD
NAVAL INSPECTOR GENERAL

SUBJECT: Independent Auditor's Report on the Attestation of the Existence, Completeness, Rights and Obligations, and Presentation and Disclosure of the Department of the Navy's Ordnance (Report No. DODIG-2014-047)

We are providing this report for information and use. No written response to this report was required. Therefore, we are publishing this report in final form.

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 601-5945.

A handwritten signature in cursive script that reads "Lorin T. Venable".

Lorin T. Venable, CPA
Assistant Inspector General
Financial Management and Reporting





**INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
4800 MARK CENTER DRIVE
ALEXANDRIA, VIRGINIA 22350-1500**

March 25, 2014

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)/
CHIEF FINANCIAL OFFICER, DOD
ASSISTANT SECRETARY OF THE NAVY (FINANCIAL
MANAGEMENT AND COMPTROLLER)

SUBJECT: Independent Auditor's Report on the Attestation of the Existence, Completeness, Rights and Obligations, and Presentation and Disclosure of the Department of the Navy's Ordnance (Report No. DODIG-2014-047)

Audit Opinion

We have examined management's assertion of audit readiness¹ for the existence, completeness, rights and obligations, and presentation and disclosure of the Department of the Navy's (DON's)² ordnance as of June 30, 2013. The DON limited its assertion by excluding ordnance in the physical custody of the Army on February 28, 2013, and we excluded ordnance outside the contiguous United States and on ships and submarines.³ DON management is responsible for its assertion of audit readiness. Our responsibility is to express an opinion on the assertion based on our examination.

We conducted our examination in accordance with attestation standards established by the American Institute of Certified Public Accountants and generally accepted government auditing standards as stated in the Government Accountability Office's "Government Auditing Standards," December 2011. Those standards require examining, on a test basis, evidence supporting the DON's assertion of audit readiness of the existence, completeness, rights and obligations, and presentation and disclosure of its mission-critical assets and performing other procedures we considered necessary. We believe that our examination provides a reasonable basis for our opinion on management's assertion.

We performed our examination using information obtained from Naval Supply Systems Command-Global Logistics Support Ammunitions (NAVSUP GLS AMMO), Marine Corps Systems Command, and DON activities⁴ for the existence, completeness, rights and obligations, and presentation and disclosure of the DON ordnance as of June 30, 2013. The DON Ordnance Information System (OIS) is the accountable property system of record for ordnance assets. As of June 30, 2013, the DON ordnance universe in OIS consisted of to 308,692,308 assets. We tested a nonstatistical sample of 24,159,045 assets for existence, 1,791,505 assets for

¹ Audit readiness per the March 2013 DoD Financial Improvement and Audit Readiness Guidance Wave 3-Mission Critical Asset Existence and Completeness Audit.

² The Department of the Navy includes both Navy and U.S. Marine Corps activities.

³ We excluded ordnance categorized as outside the contiguous United States and "AFLOAT" in the DON's Ordnance Information System.

⁴ DON activities included activities other than NAVSUP GLS AMMO, such as, Navy Munitions Command, Continental United States East Division, Yorktown, Virginia; Marine Aviation Logistics Squadron 16, San Diego, California; and Mine Warfare Training Center, San Diego, California.

completeness, and 25,950,550 assets for rights.⁵ Examples of ordnance assets tested range from Tomahawk cruise missiles, torpedoes to sonobuoys, and gun ammunition.

The DON included financial statement presentation and disclosure in its ordnance assertion. We identified approximately \$95 million of ordnance owned by the U.S. Coast Guard during our review of the DON's approximately \$46 billion of ordnance reported on the June 30, 2013 financial statements. NAVSUP GLS AMMO personnel took corrective action and reconfigured the OIS query to remove U.S. Coast Guard ordnance from the Navy financial reporting. Additionally, they identified one other organization that reports ordnance in OIS that should not be reported on the DON financial statements and removed it from the OIS query. NAVSUP GLS AMMO personnel completed the analysis of ordnance and updated OIS queries for FY 2014 first quarter data.

Additionally, we identified a discrepancy during a reconciliation of NAVSUP GLS AMMO OIS universe of transactions to the Navy third quarter financial statements. NAVSUP GLS AMMO stated the discrepancy occurred because the "On Hand Quantity" was used instead of the "Last Reported On Hand Quantity." As a result, Navy Office of Financial Operations overstated the third quarter financial statements by 1,089,225 assets. NAVSUP GLS AMMO could not determine the dollar amount associated with the overstated assets because the "tech data file," which included the unit prices, was not saved. NAVSUP GLS AMMO personnel took corrective action by using the "Last Reported On Hand Quantity" and saving the "tech data file" for FY 2014 first quarter reporting purposes.

In our opinion, the DON assertion of audit readiness for the existence, completeness, rights and obligations, and presentation and disclosure of its ordnance as of June 30, 2013, is stated fairly in accordance with DoD Financial Improvement and Audit Readiness Guidance Wave 3-Mission Critical Asset Existence and Completeness Audit.

Internal Controls

Internal controls are important for safeguarding assets. Management designs internal controls to provide reasonable assurance that unauthorized acquisition, use, or disposition of assets will be prevented or detected and corrected in a timely manner. Although we can express a favorable opinion on the DON assertion, during our examination, we identified erroneous inventory procedures, insufficient internal controls, and a lack of supporting documentation.

During our examination, we observed the following matters of concern that we are bringing to management's attention for appropriate corrective action.

- Navy personnel were provided the quantity of assets on their count sheet while conducting the inventory. The Navy relies on the "Conventional Ordnance Stockpile Management Policies and Procedures," April 2013, for inventory accountability policies and procedures. It states that the individual conducting the inventory must not be provided the quantities from master records applicable to the inventory. Navy personnel

⁵ The audit team was able to test a large quantity of assets because each piece of ordnance is tracked individually. For example, an individual bullet counts as one asset.

stated they were unaware of the requirement. There is a higher potential for inaccurate inventory records if the quantity is identified in advance. For example, if the OIS-reported inventory is less than the physical count, personnel performing the inventory might not report the difference and could pilfer any unrecorded items. Navy personnel stated they will no longer include the quantities on the count sheet when performing inventory.

- We observed a lack of internal controls in areas of segregation of duties and conflict of interest. For example, an individual had read/write-access to OIS and direct access to ordnance storage areas. This occurred because of limited personnel availability and therefore, duties could not be properly segregated. In another example, a married couple worked at the same location and worked together on ordnance inventory discrepancies. Specifically, she had read/write-access to OIS, and he had direct access to ordnance storage areas. This occurred because Navy personnel were not aware of DoD and Navy regulations requiring them to be conscious of actions that create the appearance of impropriety or that could be perceived as unethical. As a result, personnel could circumvent internal controls. The Navy should ensure that such duties are not only segregated by function, but also reviewed to avoid potential conflict-of-interest situations. The Navy should request a waiver if it is unable to properly segregate duties or prevent a conflict of interest to comply with Navy regulations. Navy personnel reassigned duties, and the married couple no longer have a direct line of communication for ordnance.
- According to the DON "Management Reassertion for Existence, Completeness, Rights and Obligations, and Presentation and Disclosure of Department of the Navy Ordnance, Excluding Department of the Navy Ordnance in the Physical Custody of the Army," February 28, 2013, key supporting documentation is available for rights and obligations from DD Form 250 "Material Inspection and Receiving Reports" (DD 250). We requested DD 250s from DON activities and concluded the majority could not be obtained for several reasons: the Wide Area Work Flow system that maintains copies of the DD 250s has limited search capabilities, the Army maintains DD 250s when it procures the ordnance, and the Navy is not required to keep the DD 250s for more than 2 years. The DON should update its process memorandum to reflect the correct supporting documentation available for rights and obligation testing.

Improving these internal control processes will help the DON become audit ready and sustain auditable processes for future financial statement examinations.

This report is intended solely for the information and use of the Under Secretary of Defense (Comptroller)/Chief Financial Officer, DoD, and the Assistant Secretary of the Navy (Financial Management and Comptroller) and is not intended to be used and should not be used by anyone else. However, this report is a matter of public record, and its distribution is not limited.



Lorin T. Venable, CPA
Assistant Inspector General
Financial Management and Reporting

Acronyms and Abbreviations

DON	The Department of the Navy
NAVSUP GLS AMMO	Naval Supply Systems Command–Global Logistics Support Ammunitions
OIS	Ordnance Information System

Whistleblower Protection

U.S. DEPARTMENT OF DEFENSE

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