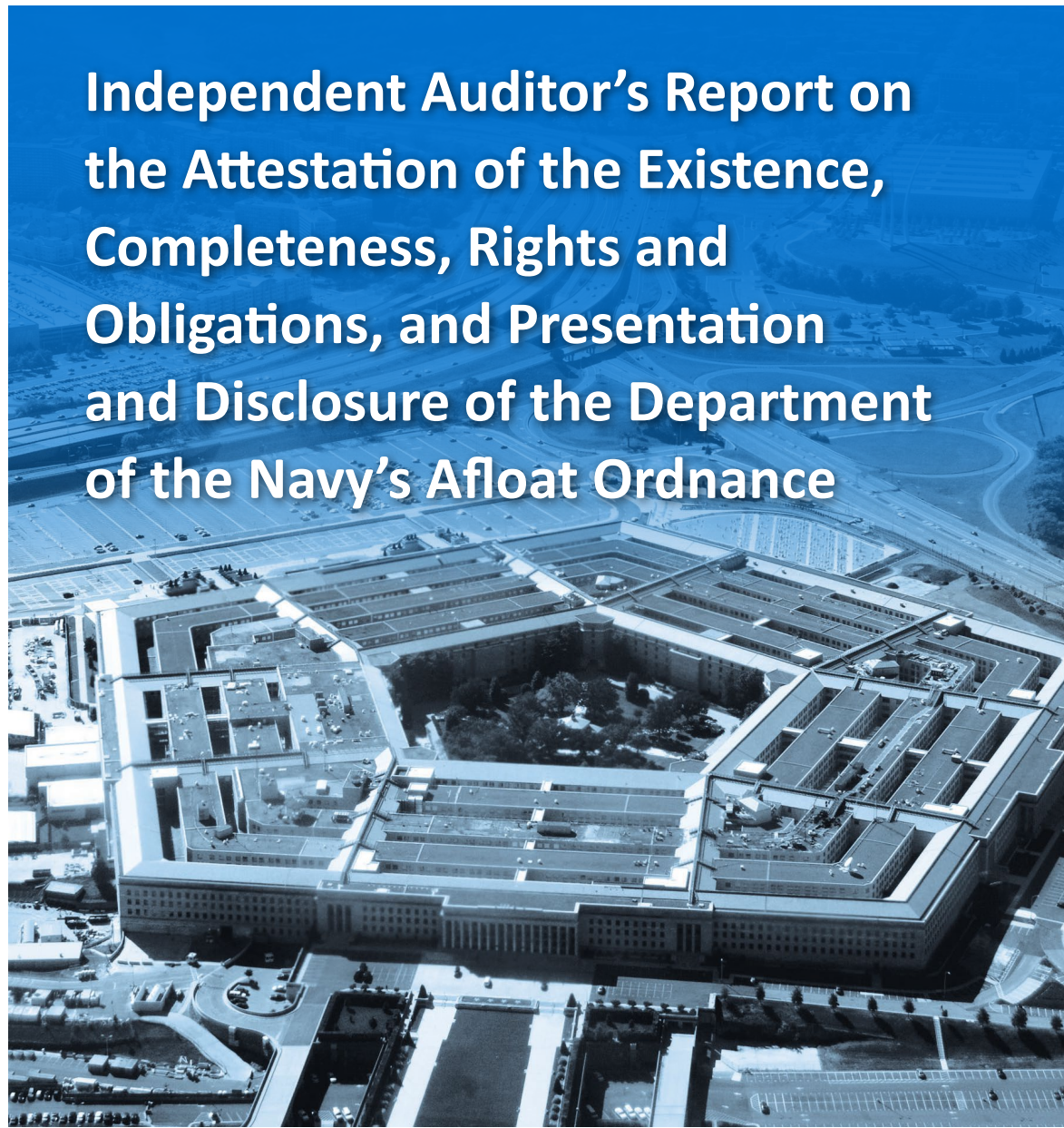




INSPECTOR GENERAL

U.S. Department of Defense

OCTOBER 2, 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 Afloat Ordnance

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

October 2, 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 Afloat Ordnance (Report No. DODIG-2015-003)

We are providing this report for information and use. No written response to this report
is 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

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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 afloat ordnance as of March 31, 2014. DON asserted audit readiness of the existence, completeness, rights and obligations, and presentation and disclosure of DON ordnance excluding that in the custody of the Army, on February 28, 2013. This examination is the second in a series of examinations of DON ordnance.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 our examination provides a reasonable basis for our opinion on management's assertion.

¹ Audit readiness in accordance with the November 2013 DoD Financial Improvement and Audit Readiness Guidance Wave 3 Mission Critical Asset Existence and Completeness Audit.

² The DON includes both Navy and U.S. Marine Corps activities.

³ We issued a report concerning DON's ordnance categorized as inside the contiguous U.S. in March 2014. Ordnance categorized as outside the contiguous U.S. in the DON's Ordnance Information System was excluded from this examination.

We performed our examination using information obtained from Naval Supply Systems Command–Global Logistics Support Ammunitions, Marine Corps Systems Command, and DON ships for the existence, completeness, rights and obligations, and presentation and disclosure of the DON afloat ordnance as of March 31, 2014. The DON Ordnance Information System (OIS)⁴ is the accountable property system of record for ordnance assets. As of March 31, 2014, the DON afloat ordnance universe in OIS consisted of 93,948,556 assets. We tested a nonstatistical sample of 584,402 assets for existence, 178,489 assets for completeness, and 763,476 assets for rights.⁵ Examples of ordnance assets tested range from Tomahawk cruise missiles and torpedoes to sonobuoys and gun ammunition.

During existence and completeness testing, we selected assets from a list that included the ship’s entire ordnance inventory. We identified the following discrepancies by comparing on-hand quantities to OIS records. For existence testing, we reviewed 584,402 assets and identified 13,303 discrepancies. For completeness testing, we reviewed 178,489 assets and identified 3,567 discrepancies. See Appendix A for more detail. A discrepancy does not always equal missing assets but can also represent record-keeping errors. When ordnance was unaccounted for, Navy had procedures to research and write-off small amounts of assets such as gun ammunition. No larger ordnance assets, such as missiles or torpedoes, were missing. As a result, our testing showed that the Navy had insignificant discrepancies between assets verified as on-hand and the quantities recorded in OIS. Some Navy commands have corrected the OIS records even though the discrepancies did not affect our opinion.

In our opinion, the DON assertion of audit readiness for the existence, completeness, rights and obligations, and presentation and disclosure of its afloat ordnance as of March 31, 2014, is stated fairly in accordance with DoD Financial Improvement and Audit Readiness Guidance Wave 3 Mission Critical Asset Existence and Completeness Audit.

Internal Controls

According to Office of Management and Budget Circular A-123, internal controls should assure the safeguarding of assets from waste, loss, unauthorized use, or misappropriation as well as assure compliance with laws and regulations. Although we can express a favorable opinion on the DON assertion, during our examination, we identified inadequate inventory procedures and insufficient internal controls.

⁴ OIS is the system of record for DON’s ordnance; however some ships still use the legacy system “Retail Ordnance Logistics Management System.” When we use the term OIS, it collectively refers to both systems.

⁵ We were 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.

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

- The Navy relied on the "Conventional Ordnance Stockpile Management Policies and Procedures," April 2014, for inventory accountability policies and procedures, which require that the individual conducting the inventory not be provided the quantities from master records applicable to the inventory. Navy personnel referred to the quantity of assets on count sheets while conducting the inventory. Navy personnel on the USS *Alaska* stated they were not aware of this requirement. As a result, there is a greater 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.
- We observed a lack of internal controls in the area of segregation of duties on the USNS *Rainier*. The Navy relied on "Conventional Ordnance Stockpile Management Policies and Procedures," April 2014. The policy states that duties are to be divided among the work force so that no individual may adversely affect the accuracy and integrity of the inventory. In addition, the policy states that key custodians must not have access to modify OIS. Lastly, the policy permits a command that is unable to comply with the separation of duties to request a waiver or an exception. On the USNS *Rainier*, we identified the following matters of concern:
 - The Assistant Cargo Mate, who had access to modify OIS, obtained keys and entered the munition storage areas unescorted. Individuals authorized to obtain keys are listed on an unescorted access control list, and these individuals must not have access to OIS. Appropriately, the Assistant Cargo Mate was not on that list, and therefore was not authorized to obtain the keys. The munition storage areas contained assets such as sonobuoys, bombs, and gun ammunition. The Assistant Cargo Mate stated this matter of concern occurred because limited personnel were available and he knew where everything was located. As a result, process integrity was not maintained, and internal controls were circumvented. The Navy should ensure that personnel cannot circumvent internal controls for reasons of convenience.
 - The Chief Mate had access to modify OIS and was authorized unescorted access to munition storage areas. Additionally, the Cargo Mate was appointed as the key custodian and was also authorized unescorted access to munition storage areas. The Assistant Cargo Mate stated these

matter of concern occurred because of limited staffing. As a result, personnel could circumvent internal controls. The Navy should request a waiver or an exception if it is unable to properly segregate duties to comply with Navy regulations. Navy personnel stated a waiver request would be submitted by the end of August 2014.

- The USS *Rushmore* did not have reliable connectivity to OIS. As the accountable property system of record for ordnance assets, OIS shows the balance of ordnance assets that the command is accountable for maintaining. The USS *Rushmore* obtained access to OIS in September 2013 and experienced frequent periods of database interruption during a ship overhaul. Navy personnel used the local area network during the overhaul and transitioned to the ship's connectivity in February 2014. Approximately 3 days after switching to the ship's connectivity, the OIS manager was unable to access the database or any functions pertaining to OIS. After repeated calls and e-mails to the OIS helpdesk, an information technology representative was sent to alleviate the problem; however, no progress was made to regain access to the OIS. As of June 4, 2014, the USS *Rushmore* was provided access to OIS via an Internet portal. This type of connectivity allows personnel to connect when they can obtain an Internet connection. When at sea, this type of connection is not always reliable and may not allow personnel to enter inventory data⁶ in accordance with Navy guidance. The Naval Supply Systems Command Headquarters—the owner of OIS—in conjunction with the Space and Naval Warfare Systems Command—the manager of the network—should ensure that this ship regains OIS connectivity as originally intended.
- During testing, we identified:
 - 29,621 assets for existence and 24,670 assets for completeness, where ordnance attributes (National Item Identification Number, Navy Ammunitions Logistic Code, and serial or lot number)⁷ were not recorded correctly. See Appendix B for more detail. This occurred because Navy personnel did not: stencil the attributes back onto assets once they wore off, update canister attributes when the canister was reused, enter the correct attribute into OIS, or know attribute information was required. As a result, Navy personnel relied on inaccurate information used to differentiate between various performance characteristics and capabilities

⁶ Inventories are performed semi-annually and annually to verify accuracy of ordnance in OIS.

⁷ A unique National Item Identification Number is given to each ordnance asset. The National Item Identification was used to calculate the dollar value of the asset. A Navy Ammunitions Logistic Code identifies ordnance items that are interchangeable. Serial and lot numbers are necessary in tracking and for performing inventory management procedures.

of different ordnance. Some Navy commands have taken corrective action and recorded attributes on the assets as appropriate. For example, all 2,640 assets for existence testing with attribute concerns aboard the USS *Carney* were corrected.

- 15,063 assets for existence and 3,810 assets for completeness where the storage location of ordnance was not properly recorded in OIS. See Appendix B for more detail. This occurred when Navy personnel who moved ordnance did not communicate storage location changes to the OIS database manager or the OIS database manager entered the storage location incorrectly into OIS. As a result, the current storage location of ordnance was not immediately known, and inventory effectiveness was compromised. Some Navy commands have taken corrective action and adjusted the storage location as appropriate. For example, all 2,396 assets for existence testing with storage location concerns aboard the USS *San Francisco* were corrected.

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

This report will be made publicly available pursuant to section 8M, paragraph (b)(1)(A), of the Inspector General Act of 1978, as amended. However, 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.



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

Appendix A

Unmatched Asset Results by Ship (Existence)

Ship	Quantity of Assets Selected	Quantity of Unmatched Assets
USNS <i>Rainier</i> (T-AOE-7)	3,843	2
USS <i>Alaska</i> (SSBN-732)	4,741	0
USS <i>Albany</i> (SSN-753)	2,338	0
USS <i>Anzio</i> (CG-68)	5,143	2
USS <i>Carl Vinson</i> (CVN-70)	125,944	3,524
USS <i>Carney</i> (DDG-64)	5,529	6
USS <i>Farragut</i> (DDG-99)	7,426	6
USS <i>Florida</i> (SSGN-728)	2,994	0
USS <i>Helena</i> (SSN-725)	1,071	0
USS <i>John Paul Jones</i> (DDG-53)	6,292	0
USS <i>Lake Champlain</i> (CG-57)	66,208	0
USS <i>Leyte Gulf</i> (CG-55)	21,539	150
USS <i>Makin Island</i> (LHD-8)	235,123	0
USS <i>Maryland</i> (SSBN-738)	2,452	0
USS <i>Newport News</i> (SSN-750)	4,061	0
USS <i>Nimitz</i> (CVN-68)	31,175	4,004
USS <i>Rushmore</i> (LSD-47)	20,608	4,521
USS <i>San Francisco</i> (SSN-711)	2,561	2
USS <i>Sterett</i> (DDG-104)	27,110	1,072
USS <i>Tennessee</i> (SSBN-734)	2,364	5
USS <i>Winston S. Churchill</i> (DDG-81)	5,880	9
Total	584,402	13,303

Unmatched Asset Results by Ship (Completeness)

Ship	Quantity of Assets Selected	Quantity of Unmatched Assets
USNS <i>Rainier</i> (T-AOE-7)	6,609	38
USS <i>Alaska</i> (SSBN-732)	4,421	0
USS <i>Albany</i> (SSN-753)	1,278	1
USS <i>Anzio</i> (CG-68)	28,124	60
USS <i>Carl Vinson</i> (CVN-70)	36,266	779
USS <i>Carney</i> (DDG-64)	14,997	20
USS <i>Farragut</i> (DDG-99)	3,284	0
USS <i>Florida</i> (SSGN-728)	123	0
USS <i>Helena</i> (SSN-725)	242	0
USS <i>John Paul Jones</i> (DDG-53)	10,464	1,003
USS <i>Lake Champlain</i> (CG-57)	2,928	0
USS <i>Leyte Gulf</i> (CG-55)	3,216	2
USS <i>Makin Island</i> (LHD-8)	3,086	0
USS <i>Maryland</i> (SSBN-738)	994	0
USS <i>Newport News</i> (SSN-750)	3,230	0
USS <i>Nimitz</i> (CVN-68)	29,777	9
USS <i>Rushmore</i> (LSD-47)	No Testing Performed due to No Connectivity to OIS	
USS <i>San Francisco</i> (SSN-711)	3,485	0
USS <i>Sterett</i> (DDG-104)	17,685	1,655
USS <i>Tennessee</i> (SSBN-734)	776	0
USS <i>Winston S. Churchill</i> (DDG-81)	7,504	0
Total	178,489	3,567

Appendix B

Other Matters of Concern* by Ship (Existence)

Ship	Quantity of Assets Selected	Assets with Attribute Concerns	Assets with Location Concerns
USNS <i>Rainier</i> (T-AOE-7)	3,843	3	470
USS <i>Alaska</i> (SSBN-732)	4,741	126	100
USS <i>Albany</i> (SSN-753)	2,338	0	0
USS <i>Anzio</i> (CG-68)	5,143	2	116
USS <i>Carl Vinson</i> (CVN-70)	125,944	1,143	6,024
USS <i>Carney</i> (DDG-64)	5,529	2,640	1,642
USS <i>Farragut</i> (DDG-99)	7,426	2,680	0
USS <i>Florida</i> (SSGN-728)	2,994	0	2,960
USS <i>Helena</i> (SSN-725)	1,071	1	0
USS <i>John Paul Jones</i> (DDG-53)	6,292	1,027	0
USS <i>Lake Champlain</i> (CG-57)	66,208	404	648
USS <i>Leyte Gulf</i> (CG-55)	21,539	1,304	620
USS <i>Makin Island</i> (LHD-8)	235,123	200	4
USS <i>Maryland</i> (SSBN-738)	2,452	0	0
USS <i>Newport News</i> (SSN-750)	4,061	0	0
USS <i>Nimitz</i> (CVN-68)	31,175	160	63
USS <i>Rushmore</i> (LSD-47)	20,608	941	0
USS <i>San Francisco</i> (SSN-711)	2,561	2	2,396
USS <i>Sterett</i> (DDG-104)	27,110	17,270	0
USS <i>Tennessee</i> (SSBN-734)	2,364	65	0
USS <i>Winston S. Churchill</i> (DDG-81)	5,880	1,653	20
Total	584,402	29,621	15,063

* Quantity of assets included in other matters of concern results were based on the entire quantity of assets tested. For example, if the recorded number of assets was 500 and we found 250 assets had an attribute concern, all 500 assets were included in other matters of concern due to asset labeling and how the assets are recorded in OIS. Similarly, if 250 assets out of 500 assets selected were stored in an incorrect location, all 500 assets were included in other matters of concern due to how the assets are recorded in OIS.

Other Matters of Concern* by Ship (Completeness)

Ship	Quantity of Assets Selected	Assets with Attribute Concerns	Assets with Location Concerns
USNS <i>Rainier</i> (T-AOE-7)	6,609	0	0
USS <i>Alaska</i> (SSBN-732)	4,421	0	0
USS <i>Albany</i> (SSN-753)	1,278	0	0
USS <i>Anzio</i> (CG-68)	28,124	22	162
USS <i>Carl Vinson</i> (CVN-70)	36,266	1	2
USS <i>Carney</i> (DDG-64)	14,997	10,600	0
USS <i>Farragut</i> (DDG-99)	3,284	0	0
USS <i>Florida</i> (SSGN-728)	123	0	120
USS <i>Helena</i> (SSN-725)	242	1	0
USS <i>John Paul Jones</i> (DDG-53)	10,464	0	0
USS <i>Lake Champlain</i> (CG-57)	2,928	1	0
USS <i>Leyte Gulf</i> (CG-55)	3,216	0	16
USS <i>Makin Island</i> (LHD-8)	3,086	0	1
USS <i>Maryland</i> (SSBN-738)	994	0	0
USS <i>Newport News</i> (SSN-750)	3,230	2,000	0
USS <i>Nimitz</i> (CVN-68)	29,777	53	54
USS <i>Rushmore</i> (LSD-47)	No Testing Performed due to No Connectivity to OIS		
USS <i>San Francisco</i> (SSN-711)	3,485	0	3,445
USS <i>Sterett</i> (DDG-104)	17,685	11,272	10
USS <i>Tennessee</i> (SSBN-734)	776	0	0
USS <i>Winston S. Churchill</i> (DDG-81)	7,504	720	0
Total	178,489	24,670	3,810

* Quantity of assets included in other matters of concern results were based on the entire quantity of assets tested. For example, if the recorded number of assets was 500 and we found 250 assets had an attribute concern, all 500 assets were included in other matters of concern due to asset labeling and how the assets are recorded in OIS. Similarly, if 250 assets out of 500 assets selected were stored in an incorrect location, all 500 assets were included in other matters of concern due to how the assets are recorded in OIS.



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U.S. DEPARTMENT OF DEFENSE

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For more information about DoD IG reports or activities, please contact us:

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