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Loss of Accounting Integrity in Air Force Procurement Appropriations. FGMSD-77-81; B-132900. November 1, 1977. 12 pp.

Report to Rep. George H. Mahon, Chairman, House Committee on Appropriations; by Robert F. Keller, Acting Comptroller General.

Issue Area: Accounting and Financial Reporting (2800).
Contact: Financial and General Management Studies Div.
Budget Function: Miscellaneous: Financial Management and Information Systems (1002).
Organization Concerned: Department of the Air Force.
Congressional Relevance: House Committee on Appropriations.
Authority: Anti-Deficiency Act (31 U.S.C. 665). Budget and Accounting Procedures Act of 1950.

The Air Force's use of improper accounting procedures has resulted in a loss of integrity in its procurement appropriations. Although the Air Force has directed that several corrective actions be taken, there is still a need to change its accounting procedures so that advances received from foreign countries under cooperative logistics arrangements are properly recorded and that such advances now in the wrong accounts are transferred to the proper accounts. Recommendations: The Secretary of Defense should have the Secretary of the Air Force direct the Air Force Audit Agency to review the revised accounting procedures the Air Force has implemented to: determine if they are adequate so that customer orders and related obligations are recorded in the proper fiscal year; determine whether it is feasible to correct prior year fund resource balances resulting from the improper customer order accounting procedures; verify that the improper entries in the fiscal year 1973 missile account have been corrected and determine the validity of adjustments made in fiscal year 1977 which increased fund resources in that account; and determine whether unobligated customer order balances in the expiring fiscal year 1975 accounts were properly transferred at the end of fiscal year 1977 and whether amounts improperly transferred at the end of fiscal years 1975 and 1976 have been recorded in the correct accounts. The Secretary of Defense should also have the Secretary of the Air Force revise Air Force accounting procedures so that the correct appropriation or stock fund is credited for advances received under cooperative logistics arrangements and adjust any advances not currently recorded in the proper account. (SC)

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**REPORT TO THE HOUSE
COMMITTEE ON APPROPRIATIONS
REPORT OF THE
COMPTROLLER GENERAL
OF THE UNITED STATES**

*Released
11/28/77*



Loss Of Accounting Integrity In Air Force Procurement Appropriations

Because improper accounting procedures were used for several years, the Air Force does not know the status of its 18 procurement appropriations from fiscal years 1971 through 1976. Consequently, it cannot determine whether it has obligated or expended more fund resources than are available in these accounts. Also, the Air Force Logistics Command recorded improper entries totaling \$7.5 million in 1976. Air Force officials told GAO this was done to avoid revealing an over-obligation in one of its procurement accounts.

The Air Force has (1) acted to correct some of the improper accounting procedures and (2) directed that the improper entries be reversed.

The Air Force should correct its procedures for recording advances received from foreign countries under cooperative logistics agreements. The Air Force Audit Agency should also evaluate the effectiveness of the revised accounting procedures and verify that the improper entries were corrected.



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-132900

The Honorable George H. Mahon, Chairman
Committee on Appropriations
House of Representatives

Dear Mr. Chairman:

Your March 17, 1977, letter requested that we find out if the Air Force has experienced financial management problems similar to those described in our November 5, 1976, report to the Congress entitled "Serious Breakdown in the Army's Financial Management Systems" (FGMSD-76-74).

Among the problems discussed in the Army report were the improper recording of foreign military sales customer orders and the resultant loss of administrative control over several procurement appropriations.

The Air Force has experienced problems similar to those of the Army which have resulted in a loss of accounting integrity in its procurement appropriations from fiscal years 1971 through 1976. Also, improper entries were made in the fiscal year 1973 Missile Procurement Appropriation account. Air Force officials told us this was done to avoid showing an overobligation in the accounting records.

SCOPE OF REVIEW

Before we initiated our review, the Air Force Audit Agency had completed a comprehensive Air Force-wide audit of the foreign military sales program's administration. The audit, which required more than 7,300 staff-days to complete, resulted in two reports dated July 9, 1976, and February 16, 1977.

These reports revealed that most of the financial management problems pertaining to foreign military sales customer orders focused on Headquarters, Air Force, and the Air Force Logistics Command. Accordingly, we restricted our review to those two organizations. To the extent practicable, we used the results of the Audit Agency's work. In addition, we

--reviewed (1) Defense and Air Force directives, manuals, and regulations on administrative control of funds and (2) Air Force records and reports; and

--interviewed cognizant Air Force and Defense officials.

BACKGROUND

The Air Force's share of foreign military sales has grown from \$419 million in fiscal year 1970 to \$5 billion in fiscal year 1976. The Air Force Logistics Command accounts for about 70 percent of the number of sales and 30 percent of the total dollar value of sales in the Department.

Procuring most material and services for foreign military sales is initially financed through various Air Force appropriations which are reimbursed as the material and services are delivered to customers. Most of the sales are financed through the Air Force's Aircraft Procurement, Missile Procurement, and Other Procurement appropriations.

To facilitate financing foreign military sales, the dollar amounts of customer orders received are treated as increases to the Air Force's obligational authority. To insure proper administrative control over appropriations, it is important that the accounting system be designed so that customer orders are recorded in the year received and that reimbursements are credited to the appropriation financing the orders.

The Budget and Accounting Procedures Act of 1950 places responsibility for establishing and maintaining adequate systems of accounting and internal control upon the head of each executive agency. Further, the Anti-Deficiency Act (31 U.S.C. 665) requires officials responsible for controlling appropriations to devise systems of administrative control which will restrict obligations and expenditures to amounts apportioned and which will enable fixing responsibility for creating any obligation or for making any expenditure in excess thereof. In letters dated May 16, 1977, to the Secretary of Defense and June 28, 1977, to other department and agency heads, the Director, Office of Management and Budget, emphasized the requirements of the act and the need to have adequate administrative controls to prevent overobligating and/or overexpending.

LOSS OF ADMINISTRATIVE CONTROL OVER
AIR FORCE PROCUREMENT APPROPRIATIONS

Because of improper procedures the Air Force Logistics Command used in accounting for foreign military sales customer orders, the Air Force does not know the correct fund balances of its three procurement appropriations for each fiscal year from 1971 through 1976. As a result, the Air Force cannot determine whether it has obligated and/or expended more fund resources than are available.

Foreign military sales cases are established when a Letter of Offer and Acceptance (DD Form 1513) is executed. The year in which the case is signed is referred to as the case year. DD Form 1513 represents authority to obligate funds on certain types of sales cases. However, under procedures implemented in fiscal year 1974, most cases assigned to the Air Force Logistics Command require a subsequent firm, definitized customer order to be received before obligational authority is established. Often they are received in fiscal years subsequent to the year in which the case was signed; obligations and earnings associated with the customer order often occur in even later years.

In 1976 the Air Force Audit Agency reported that procedures used to account for foreign military sales cases managed by the Air Force Logistics Command did not comply with the Department of Defense Accounting Guidance Handbook. Customer orders, representing obligational authority, were being recorded in the year in which the case was signed regardless of when the orders were received and accepted or when funds to fill the orders were obligated. The related earnings and collections for these orders were also being recorded in the year in which the case was signed, even though obligations were incurred to support the order in subsequent fiscal year appropriations. The Logistics Command used these procedures for at least 6 years.

The Department of Defense Accounting Guidance Handbook specifies that customer orders must be recorded in the most current appropriation account available when the orders are received. To maintain accounting control and appropriation integrity, it is imperative that subsequent related obligations, earnings, and collections be recorded in the same accounts where these orders were initially recorded.

Recording obligations in one appropriation account while recording related customer orders, earnings, and collections in another appropriation account distorts the status of those accounts. For example, the Air Force Audit Agency found that, as of November 1975, \$82.3 million in customer orders recorded in the fiscal year 1973 Air Force Aircraft procurement account (representing additional obligational authority to the appropriation) were received after fiscal year 1973. As of November 1975, \$53.2 million in obligations against these orders were recorded in fiscal year 1974, 1975, and 1976 accounts.

Logistics Command officials advised us that due to the huge volume of foreign military sales transactions and the absence of key data elements in the records for prior year transactions, it would be impossible to correct the accounts for reimbursements which were recorded in the wrong appropriation year.

Since the practice of recording customer orders in the wrong appropriation account apparently involved hundreds of millions of dollars in fiscal years 1971 through 1976 procurement appropriations, correcting adjustments, if they could be made, might drastically change the amounts of resources available in any or all of those accounts.

As indicated in the following schedule, several of the procurement appropriations have relatively small fund balances available. Consequently, adjustments to those accounts might show them to be in an overobligated status.

Status of Procurement Appropriations
July 31, 1977

<u>Procurement appropriation</u>	<u>Year</u>	<u>Status</u>		<u>Unobligated balance available</u>
		<u>Resources (note a)</u>	<u>Obligations</u>	
(millions)				
3010-Aircraft	b/M	\$ -	-	\$ 63.0
	1973	3,478.5	3,469.5	9.0
	1974	3,937.4	3,883.9	53.5
	1975	4,539.4	4,348.5	190.9
	1976	6,785.7	5,817.0	968.7
	1977	6,800.6	4,030.4	2,770.2
3020-Missile	b/M	\$ -	\$ -	\$ 84.0
	1973	1,691.6	1,687.6	c/4.0
	1974	1,499.2	1,489.7	9.5
	1975	1,555.9	1,511.3	44.6
	1976	1,968.0	1,804.8	163.2
	1977	2,021.0	1,072.7	948.3
3080-Other	b/M	\$ -	\$ -	\$ 7.7
	1973	2,103.5	2,100.6	2.9
	1974	1,733.3	1,710.0	23.3
	1975	1,815.0	1,698.3	116.7
	1976	2,519.4	2,248.0	271.4
	1977	2,477.1	1,406.3	1,070.8

a/Resources include funds appropriated by the Congress for direct Air Force programs plus the total value of reimbursable orders received.

b/1972 and all prior year accounts.

c/The fiscal year 1973 missile account is discussed further on p. 6.

According to Air Force auditors, the Air Force was aware in fiscal year 1973 that reimbursements were not being recorded correctly. Even though Air Force officials knew for several years that there was a weakness in administrative controls over reimbursements, they told us that prompt action was not taken to correct the problem because a moratorium had been placed on system changes. This was due to the high priority given to developing the Advanced Logistics System.

Under new procedures implemented on October 1, 1976, customer orders, earnings, collections, and related obligations are now required to be recorded in the same appropriation year account. We did not evaluate these new procedures during our review.

We believe the Air Force Audit Agency should review the new accounting procedures and also determine whether adjustments to correct improper recording of customer orders from fiscal years 1971 through 1976 are possible or feasible. (See p. 11.)

IMPROPER AUGMENTATION OF THE FISCAL YEAR
1973 MISSILE PROCUREMENT ACCOUNT

In June and July 1976, the Air Force Logistics Command recorded a series of accounting entries which resulted in the improper transfer of about \$7.5 million in earnings and collections from the fiscal year 1975 aircraft procurement account to the fiscal year 1973 missile procurement account. Air Force officials told us the entries were made to avoid showing an overobligation in the accounting records for the fiscal year 1973 missile procurement account.

From July 1, 1972, to June 30, 1975, the Air Force Logistics Command recorded customer orders valued at \$7.5 million related to a particular foreign military sales case in the fiscal year 1973 missile procurement account. Since these unfilled orders ^{1/} represented obligational authority, fund resources in the account were thereby increased by \$7.5 million. After recording these unfilled orders, however, the Logistics Command changed its criteria for determining which appropriation would be credited with earnings and collections realized from customer orders. The change was necessary to correct a systems deficiency which was causing some customer orders, earnings, and collections related to foreign military sales to be recorded in appropriations different from the appropriations where related obligations were recorded. This distorted the status of the appropriation accounts involved.

As a result of this systems change, earnings and collections related to the \$7.5 million in unfilled orders recorded in the fiscal year 1973 missile account were required

^{1/}Unfilled orders are amounts of foreign military sales orders received for which no earnings have yet been realized.

to be recorded in the fiscal year 1973 aircraft account. As the latter recordings were made the unfilled orders (and thus fund resources) were eliminated from the missile account. However, obligations for other purposes were already being incurred in the missile account under the assumption that \$7.5 million in resources would be realized. As a result, obligations were almost exceeding obligational authority in the missile account. If this did happen, a violation of the Anti-Deficiency Act would have occurred.

Air Force officials told us that, to prevent such an overobligation from showing on accounting records, the Air Force transferred \$7.5 million in earnings and collections from the fiscal year 1975 aircraft appropriation account to the fiscal year 1973 missile account. Officials also told us that the transfer was made because they did not feel that an account should be overobligated because of a systems change intended to improve accounting procedures.

We agree that this change was necessary to correct a system deficiency. The effect of the change on the \$7.5 million in reimbursements discussed above was to put the earnings and collections in the proper account--where the related obligations were recorded. We see no basis, however, for the subsequent Air Force action moving earnings and collections back to the wrong account to avoid showing an overobligation in the accounting records.

On September 14, 1977, after we suggested that the above entries be reversed, Headquarters, Department of the Air Force, directed the Air Force Logistics Command to record entries to return the \$7.5 million in reimbursements from the missile account to the aircraft account before September 30, 1977.

Air Force officials told us that because adjustments to the fiscal year 1973 missile appropriation account since our review resulted in increased fund resources, it seems that removing the \$7.5 million in reimbursements will not cause a fund deficiency.

We believe the Air Force Audit Agency should review the recent adjustments which increased available resources in the fiscal year 1973 missile account and verify that the \$7.5 million in reversals were recorded by the Air Force. (See p. 11.)

IMPROPER TRANSFERS OF UNFILLED,
UNOBLIGATED CUSTOMER ORDER BALANCES

During its 1975 and 1976 fiscal yearend closeout and adjusting process, the Air Force recorded entries which improperly transferred to current procurement accounts from expiring accounts \$64 million in unobligated fund resources related to customer orders.

Frequently, all obligations necessary to completely fill various foreign military sales orders have not been incurred by the time the account expires for obligational purposes. To be able to use remaining obligational authority to complete filling these orders, the related unobligated balances must be moved out of the expiring account to a current account.

To do this, the Department of Defense Accounting Guidance Handbook provides that, in the case of expiring appropriation accounts,

"* * * balances of uncollected unearned (or unobligated) but still valid customer orders will be eliminated from the expiring (or expired) account and recorded under the ensuing fiscal year account
* * *."

Department of Defense officials informed us that the intent of this provision is to allow moving unobligated balances related to customer orders out of expiring accounts into the most current year account of that appropriation. For example fiscal year 1973 procurement appropriation accounts, each of which had a 3-year life, expired at the end of fiscal year 1975. Defense requires unobligated balances in an expiring fiscal year 1973 procurement account to be moved to the corresponding fiscal year 1976 procurement account.

Under this provision, the Air Force has moved large amounts of fund resources from expiring accounts to more current accounts. However, rather than consistently moving these balances to the ensuing fiscal year account, they have been arbitrarily moved to any of the three current accounts for that appropriation. The following examples illustrate this.

At the end of fiscal year 1976, the fiscal year 1974 procurement appropriation accounts were expiring for obligational purposes. The Air Force determined that there was a total of \$46.1 million in customer order unobligated

balances in the expiring accounts and made the following transfers:

<u>Expiring fiscal year 1974 procurement account from which unobligated balances were moved</u>	<u>Amount</u>	<u>Fiscal year account to which unobligated balances were moved</u>
	(millions)	
3010-Aircraft	\$36.5	1975
3020-Missile	1.9	1976
3080-Other	7.7	1977

At the end of fiscal year 1975, when the fiscal year 1973 procurement accounts were expiring, \$26 million in customer order unobligated balances were moved to accounts other than the fiscal year 1976 accounts.

Under the Department of Defense provision for moving forward unobligated balances, amounts in expiring fiscal year 1974 procurement accounts should have been moved to the related fiscal year 1977 accounts. Amounts in expiring fiscal year 1973 procurement accounts should have been moved to the related fiscal year 1976 accounts.

As a result of these entries, some fiscal year 1975 and 1976 accounts have overstated fund resource balances while other fiscal year 1976 and 1977 accounts have understated fund resource balances.

Because these transfers of fund resources did not meet the intent of the Department of Defense Accounting Guidance Handbook provisions, we suggested that the Air Force adjust the appropriation accounts involved to reflect balances which would exist had the original transfers been made to the most current accounts. On September 14, 1977, Headquarters, Air Force, directed that unfilled, unobligated customer order balances moved improperly at the end of fiscal years 1975 and 1976 be moved to the correct fiscal year before September 30, 1977.

We believe the Air Force Audit Agency should determine whether these customer order unobligated balances are now being transferred properly and whether amounts improperly transferred in the past have been corrected. (See p. 11.)

APPROPRIATION FUND RESOURCES DISTORTED
BY IMPROPER CREDIT OF REIMBURSEMENTS

Because the Air Force Logistics Command used improper procedures to record advances received from foreign countries under cooperative logistics arrangements, fund resources in the Aircraft Procurement Appropriation are overstated by an estimated \$50 million and fund resources in other accounts are understated by a similar amount.

Under cooperative logistics arrangements foreign countries invest in military services' inventories by advancing cash to cover a substantial portion of the estimated cost of providing supplies over a 17-month period. These advances are used to fund the initial anticipated supply requirements of foreign countries for the first 5 months of the case.

The Air Force is not recording the advances in the correct appropriation. Its procedures require that all reimbursement advances received under cooperative logistics arrangements be credited to the Aircraft Procurement Appropriation. This is improper because other appropriations and stock funds, such as the Missile Procurement Appropriation and the Air Force Stock Fund, are also used to finance cooperative logistics arrangements.

As of August 1977, advances to the Air Force under cooperative logistics arrangements which are renegotiated periodically, totaled an estimated \$98 million. Through examining logistics sales data we estimate that roughly \$50 million should have been credited to appropriations and funds other than the Aircraft Procurement Appropriation.

According to the Air Force, as of September 30, 1977, it has not determined whether action will be taken to change its procedures so that the advances are recorded in the proper account.

CONCLUSIONS

The Air Force's use of improper accounting procedures has resulted in a loss of integrity in its procurement appropriations.

Although the Air Force has directed that several corrective actions be taken there is still a need to change its accounting procedures so that advances received from

foreign countries under cooperative logistics arrangements are properly recorded and that such advances now in the wrong accounts are transferred to the proper accounts.

Further, there is a need for the Air Force Audit Agency to determine whether (1) the Air Force has properly implemented its new accounting procedures, (2) those procedures are adequate, and (3) the accounting adjustments directed by Headquarters, Air Force, were properly recorded. Also the Agency should find out whether it is feasible for the Air Force to correct the errors in accounting records for fiscal years 1971 through 1976 procurement appropriations which were caused by recording orders and related obligations in different years.

RECOMMENDATIONS

We recommend that the Secretary of Defense have the Secretary of the Air Force direct the Air Force Audit Agency to

- review the revised accounting procedures the Air Force implemented on October 1, 1976, to determine if they are adequate so that customer orders and related obligations are recorded in the proper fiscal year,
- determine whether it is feasible to correct prior year fund resource balances resulting from the improper customer order accounting procedures,
- verify that the \$7.5 million in improper entries in the fiscal year 1973 missile account have been corrected and determine the validity of adjustments made in fiscal year 1977 which increased fund resources in that account,
- determine whether unobligated customer order balances in the expiring fiscal year 1975 accounts were properly transferred at the end of fiscal year 1977 and whether amounts improperly transferred at the end of fiscal years 1975 and 1976 have been recorded in the correct accounts.

We also recommend that the Secretary of Defense have the Secretary of the Air Force revise Air Force accounting procedures so that the correct appropriation or stock fund

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is credited for advances received under cooperative logistics arrangements and to adjust any advances not currently recorded in the proper account.

We discussed our findings with Air Force and Department of Defense officials and where appropriate their comments are included in the report.

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As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House Committee on Government Operations and the Senate Committee on Governmental Affairs not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report. After the report has been issued, we will contact your office to arrange for further distribution of the report so that these requirements can be met.

Sincerely yours,

ACTING Comptroller General
of the United States

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