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Correct Balance of Navy's Foreign Military Sales Trust Fund Unknown. FGMSD-79-2; B-132900. November 15, 1978. Released November 15, 1978. 8 pp.

Report to Rep. George H. Mahon, Chairman, House Committee on Appropriations; by Elmer B. Staats, Comptroller General.

Issue Area: Accounting and Financial Reporting; Overobligations and Overexpenditures (2804).

Contact: Financial and General Management Studies Div.

Budget Function: Miscellaneous: Financial Management and Information Systems (1002).

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Congressional Relevance: House Committee on Appropriations. Rep. George H. Mahon.

Authority: 31 U.S.C. 200.

The Navy's foreign military sales (FMS) trust fund account is used to hold and account for cash collected for foreign countries until it is disbursed. The Department of the Treasury maintains trust fund records, but balances on those records result from data reported to it by the services. Cash collections and disbursements are accounted for in detailed sales case accounting records which are maintained by the Defense Department's Security Assistance Accounting Center. The Center is also responsible for managing the trust fund.

Findings/Conclusions: Problems in the Navy's accounting and reporting of FMS disbursements and collections were disclosed when the sales case accounting records were transferred to the Center. The Navy was directed to reconcile the cash balance on the trust fund records with the cash balance shown on official detailed sales case accounting records. Despite more than a year's effort involving thousands of staffdays, the Navy has not been able to reconcile these balances. As a result, the correct amount of cash being held for foreign countries is not known. Some of the adjustments made by the Navy were in error or were not adequately supported. Differences between the Treasury trust fund and sales case accounting records have continued to increase, and, at June 1, 1978, totaled \$554 million. Under the Navy's current system, there will continue to be a significant amount of transactions in-float at any time, and, therefore, there will continue to be differences in the balances.

Recommendations: The Secretary of Defense should have the Secretary of the Navy direct that prompt action be taken to determine the trust fund cash balance that can be documented for each foreign country and require that Treasury records and sales case accounting records be adjusted accordingly; and insure that procedures are implemented to identify transactions in-float so that in the future the Treasury trust fund balance can be regularly reconciled to sales case accounting records. The

Secretary of Defense should direct the Defense Audit Service to review and report to him whether: all adjustments to Treasury trust fund and sales case accounting records are valid, the Treasury trust fund and sales case accounting record balances have been effectively reconciled and are accurate, and procedures have been implemented to enable regular reconciliations of the two sets of records in the future.  
(Author/HTW)

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REPORT BY THE  
**Comptroller General**  
OF THE UNITED STATES

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## Correct Balance Of Navy's Foreign Military Sales Trust Fund Unknown

*released*  
*11-15-78*

The Department of Defense does not know the correct cash balance being held in trust for countries involved in the Navy's foreign military sales program. This is despite the Navy's having spent thousands of staff days since early 1977 to determine why the trust fund account does not agree with detailed military sales case accounting records. Unreconciled differences in cash balances between the two sets of records totaled \$554 million, as of June 1, 1978.

GAO recommends that the Navy

- determine the correct trust fund cash balance,
- record appropriate adjustments to financial records, and
- develop procedures which will enable periodic reconciliations of the trust fund and case accounting records in the future.

GAO also recommends that the Defense Audit Service verify the validity of adjustments to the Treasury trust fund and to sales case accounting records.





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

B-132900

November 15, 1978

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 Navy has experienced financial management problems in administering the foreign military sales program. As agreed with your office, we directed our efforts primarily toward reviewing the Navy's accounting system for moneys which foreign governments have, in accordance with sales agreements, deposited in the foreign military sales trust fund account. The Navy uses these moneys to cover disbursements for military goods and services it purchases for foreign governments.

We found large unreconciled differences between the foreign military sales disbursement and collection data reported by the Navy to the Department of the Treasury (which maintains the trust fund) and to Defense's Security Assistance Accounting Center (which maintains detailed sales case accounting records). As a result, for some time the Treasury and the Center have shown different cash balances on their records. For example, cash balances on the Center's sales case accounting records, as of June 1, 1978, were \$554 million more than the cash balances on the Treasury's records. Until the Navy can reconcile the difference in disbursements and collections it has reported to the two organizations, the correct balances deposited in trust by foreign governments cannot be determined. Also, the Navy needs to improve its accounting system so that future differences in reported disbursement data can be promptly reconciled.

#### SCOPE OF REVIEW

Our review was made at Headquarters, Department of the Navy, Washington, D.C.; the U.S. Navy International Logistics Control Office, Philadelphia, Pennsylvania; and the Security Assistance Accounting Center, Denver, Colorado. We examined trust fund and sales case records and reviewed pertinent Defense and Navy regulations. We also interviewed responsible Defense and Navy officials.

#### BACKGROUND

The foreign military sales program has grown from less than \$1 billion in fiscal year 1970 to about \$11.2 billion

in fiscal year 1977. Defense financial management systems were not designed to accommodate such phenomenal growth of the program. The adverse effects of this growth on Army and Air Force financial operations were included in three reports to you entitled "Serious Breakdown in the Army's Financial Management Systems" (FGMSD-76-74) November 5, 1976; "Loss of Accounting Integrity in Air Force Procurement Appropriations" (FGMSD-77-81) November 1, 1977; and "Army Efforts To Restore Integrity to Its Financial Management Systems" (FGMSD-78-28) April 27, 1978. This is our initial report to you on the Navy's financial management problems.

The Navy's portion of foreign military sales cases for fiscal year 1977 amounted to over \$2 billion. Administering sales cases usually involves numerous cash collections (advances, payments, etc.) from the foreign countries and payments to the sources which provide the material or service purchased. A foreign military sales trust fund account is used to hold and account for the cash collected from foreign countries until it is paid out. The Department of the Treasury maintains trust fund records; however, the balances on those records result from collection and disbursement data reported to it by the services.

Cash collections and disbursements are also accounted for in detailed sales case accounting records. Effective in February 1977, responsibility for maintaining all of the official sales case accounting records was transferred from the Navy to the Defense Department's Security Assistance Accounting Center. The Center, which was established by the Secretary of Defense in September 1976 to serve as a central operation for foreign military sales billing and collecting, was also given full responsibility for managing the trust fund.

The cash balance in the Treasury's trust fund account determines the amount of money that can be disbursed for military goods and services sold to each foreign country. The sales case accounting records are used to render an accounting to each foreign country as to what its cash balance is. It is, therefore, very important that any difference between the cash balances shown on the two sets of records be promptly and properly reconciled.

PROBLEMS DISCLOSED WHEN RECORDS  
TRANSFERRED TO SECURITY ASSISTANCE  
ACCOUNTING CENTER

The Navy's problems in accounting and reporting foreign military sales disbursements and collections were disclosed when the Navy International Logistics Control Office was required to transfer official detailed sales case accounting records to the Center. At that time the Navy was directed by Defense to reconcile the cash balance shown on the trust fund records with the cash balance shown on official detailed sales case accounting records.

Using May 31, 1977, individual sales case accounting record and trust fund balances, the Navy found that cash balances for 26 countries were \$58 million higher on the trust fund account than on individual sales case accounting records, and cash balances for 42 countries were \$145.3 million higher on individual sales case accounting records than on the trust fund account.

The Navy's calculations also showed that although there were some variances in collection totals recorded on the two sets of records, most of the differences in cash balances were a result of variances in recorded disbursements. Accordingly, the Navy decided to limit its initial reconciliation efforts to determining why disbursements on Treasury records differed by so much from disbursements on sales case accounting records.

In examining the reasons for the differences, the Navy found that a significant amount of disbursements which had been recorded against the trust fund cash balance had not been recorded in individual sales case accounting records. Under the Navy's disbursement accounting and reporting system, regional finance centers submit monthly reports to Navy headquarters which include summary disbursement data for foreign military sales. The headquarters in turn submit the data to the Treasury for posting to the trust fund account. Regional finance centers also provide detailed disbursement data on a daily basis to the Navy International Logistics Control Office for posting to individual sales case accounting records. The Navy found that it was taking considerably longer to post disbursements to the individual sales case accounting records than it took the Treasury to post summary disbursement data to the trust fund account. Primarily by identifying disbursements which were "in-float" (i.e., those disbursements not recorded in the detailed sales case accounting records), the Navy was able to make large

adjustments to the differences in cash balances. However, despite these adjustments, at June 1, 1978, after approximately 3,000 Navy staffdays had been used in the reconciliation, total cash balances for 31 countries were still \$9.4 million higher on individual sales case accounting records than on the Treasury's books, and cash balances for 37 countries were still \$153.5 million higher on the Treasury's books than on individual sales case accounting records.

Since all in-float transactions should have been recorded long before June 1, 1978, other causes for the cash balance differences had to be identified. At the time we completed our review, the Navy was continuing its reconciliation effort by examining individual sales case accounting records for any errors that might have been made in recording financial data.

Reconciliation procedures and methods needed improvement

During our review, we made a limited check of the ongoing reconciliation and found that, because written procedures had not been developed and questionable methods were being used to reconcile the cash balances, some of the accounting adjustments made by the Navy were not adequately supported or were in error. We found that:

1. Reconciliation procedures were not adequately documented. For the most part, clerks were instructed orally on reconciliation procedures to be used. As a result, procedures had often been inconsistently applied and differences in cash balances for various countries had been computed using different methods.
2. Reconciliation work was often not adequately supported with documentation and did not provide an audit trail. Also, figures on reconciliation worksheets were often changed without written explanation and did not always agree with balances reported by the Logistics Control Office to Navy headquarters.
3. There was an apparent tendency to apply expenditure transactions to differences in cash balances as of May 31, 1977, even though transaction dates were not readily apparent. Our research on some of these items showed that transaction dates were later than May 31, 1977.
4. The method used by the Navy to reconcile the cash balances assumed that the cash balance recorded in the Treasury trust fund was correct and that all adjustments therefore

should be made to the sales case accounting records. The Navy cannot support this assumption. The trust fund account was established about 20 years ago and, in all likelihood, over the years at least some disbursements have been erroneously charged against or omitted from the fund.

During our review, we notified Navy officials of the problems found with reconciliation procedures and the erroneous or unsupported accounting adjustments recorded during the reconciliation. Navy officials said that appropriate corrective action would be taken.

DIFFERENCES BETWEEN INDIVIDUAL SALES CASE ACCOUNTING RECORDS AND TRUST FUND ACCOUNT BALANCES HAVE INCREASED TO \$554 MILLION

As stated above, since the Navy transferred foreign military sales case accounting records and administrative control over related trust fund cash balances, the Security Assistance Accounting Center has been responsible for maintaining individual sales case accounting records and issuing bills to foreign countries.

The Navy continues to make disbursements for its foreign sales cases by directly charging the trust fund. It reports disbursement data monthly to the Treasury. Since the Security Assistance Accounting Center is now the custodian of official sales case accounting records, the Navy must also report disbursements through the Navy International Logistics Control Office to the Center for posting to individual sales case accounting records.

The extra step in reporting disbursements has contributed to additional delays in recording them on case records. Also, according to Navy officials, the Control Office is experiencing delays in reporting disbursement data to the Center because it is having problems implementing a new accounting system for foreign military sales.

As a result, while the Navy has been trying to reconcile the differences in cash balances between the Treasury's trust fund account and individual sales case accounting records identified as of May 31, 1977, differences have continued to increase since that date. For example, at June 1, 1978, the Treasury trust fund cash balance was \$876.4 million while cash balances on individual sales case accounting records at the Accounting Center totaled \$1,430.9 million, a difference of \$554.5 million.



Accounting Center officials acknowledged that a substantial portion of this difference was probably due to disbursement transactions in-float, that is, disbursements recorded in the Treasury's trust fund account but not yet reported to the Center by the Navy International Logistics Control Office. They added, however, that until the Navy identifies those transactions it has reported to the Treasury which have not yet been reported to the Accounting Center, they will not be able to reconcile individual sales case accounting records to the trust fund or to determine the correct amount of cash being held in trust for foreign countries.

As part of its new accounting system for foreign military sales, the Navy has been trying for some time to develop a mechanized report of disbursement transactions in-float, but it has been unsuccessful. The mechanized report would identify those foreign military sales disbursement transactions which have been reported to the Navy International Logistics Control Office by Navy regional finance centers but which have not been reported to the Accounting Center for posting to sales case accounting records. Navy officials advised us that the mechanized report will be available for use before the end of calendar year 1978.

On August 7, 1978, the Comptroller of the Defense Security Assistance Agency notified the Assistant Secretary of the Navy (Financial Management) that because of the large amounts of trust fund disbursement transactions in question, until the Navy was able to provide information necessary to reconcile the trust fund account and individual sales case accounting records, he could not certify to the accuracy of trust fund account balances pursuant to 31 U.S.C. 200.

Defense has recognized the seriousness of this problem. In May 1978 the Defense Steering Committee for Prioritization of Foreign Military Sales Financial Management Implementation designated the problem in reconciling the Navy's trust fund account balances as the top priority issue facing Defense in improving its financial management of the foreign sales program.

### CONCLUSIONS

Despite more than a year's effort involving thousands of staffdays, the Navy has not been able to reconcile the Treasury's trust fund cash balance to individual sales case accounting record cash balances. As a result, the correct amount of cash being held for foreign countries is not known. Also, some of the adjustments made by the Navy were in error

or were not adequately supported. Further, differences between the Treasury trust fund and sales case accounting records have continued to increase since May 31, 1977, and, at June 1, 1978, totaled \$554 million.

The Navy should take prompt action to determine the trust fund cash balances that can be documented for each foreign country and see to it that Treasury records and sales case accounting records are adjusted to reflect those balances.

Under the Navy's current system of making disbursements for foreign military sales and reporting those disbursements to the Security Assistance Accounting Center, there will continue to be a significant amount of transactions in-float at any point in time, and therefore there will continue to be differences between the Treasury trust fund and sales case accounting record balances. The Navy should implement procedures to identify in-float transactions so that in the future the Treasury trust fund can be regularly reconciled to sales case accounting records.

The Defense Audit Service should be directed to review and report to the Secretary of Defense whether (1) all adjustments to Treasury trust fund or sales case accounting records are valid, (2) the Treasury trust fund and sales case accounting records have been effectively reconciled, and (3) procedures have been developed to enable regular reconciliations of the two sets of records in the future.

#### RECOMMENDATIONS

We recommend that the Secretary of Defense have the Secretary of the Navy

--direct that prompt action be taken to determine the trust fund cash balance that can be documented for each foreign country and require that Treasury records and sales case accounting records be adjusted accordingly and

--insure that procedures are implemented to identify transactions in-float so that in the future the Treasury trust fund balance can be regularly reconciled to sales case accounting records.

We also recommend that the Secretary of Defense direct the Defense Audit Service to review and report to him whether (1) all adjustments to Treasury trust fund and sales case accounting records are valid, (2) the Treasury trust fund and sales case accounting record balances have been effectively reconciled and are accurate, and (3) procedures have

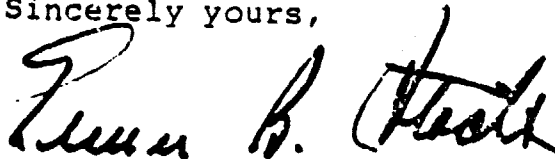
been implemented to enable regular reconciliations of the two sets of records in the future.

As agreed with your office, we did not obtain written comments but discussed our findings with Navy and Defense officials and their comments have been considered in the preparation of this 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,



Comptroller General  
of the United States