

GAO

Report to the Under Secretary of
Defense (Comptroller), the Assistant
Secretary of the Navy for Financial
Management, and the Director of the
Defense Finance and Accounting Service

July 1996

CFO ACT FINANCIAL AUDITS

Navy Plant Property Accounting and Reporting Is Unreliable



G A O
75 years
1921 - 1996



United States
General Accounting Office
Washington, D.C. 20548

Accounting and Information
Management Division

B-271580

July 8, 1996

The Honorable John J. Hamre
The Under Secretary of Defense (Comptroller)

The Honorable Deborah P. Christie
The Navy Assistant Secretary for
Financial Management
and Comptroller

Mr. Richard F. Keevey
Director, Defense Finance and
Accounting Service

On March 27, 1996, we reported¹ on the results of our review of the reliability of the Navy's fiscal year 1994 consolidated financial reports on general fund operations. These financial reports, submitted to the Department of the Treasury, included \$78 billion for the Navy's plant property, comprising (1) land, structures, and facilities, (2) nonmilitary equipment at shore activities, (3) nonmilitary equipment the Navy has paid for but not yet received, and (4) incomplete capital improvements to existing Navy-owned buildings. The last two items are referred to by the Navy as plant property work-in-progress.

At that time, we advised you that these financial reports were substantially inaccurate due to a minimum of \$225 billion in errors covering many different areas, including at least \$25.6 billion in errors involving the Navy's plant property account balance. We also made more than a dozen recommendations to avoid the mistakes made in preparing the Navy's fiscal year 1994 consolidated financial reports on general fund operations.

This report describes in greater detail the areas contributing to inaccurate financial reporting of the Navy's plant property account balance. It also recommends additional actions needed to further help ensure that the Navy has reliable information to effectively manage and adequately control the billions of dollars the government has invested in the Navy's plant property.

¹CFO Act Financial Audits: Increased Attention Must Be Given to Preparing Navy's Financial Reports (GAO/AIMD-96-7, March 27, 1996).

Results in Brief

The credibility and usefulness of the Navy's plant property financial information was greatly diminished by the following four weaknesses that contribute to, and are generally caused by, the basic deficiencies underlying the Navy's substantial financial reporting problems we reported in March 1996. First, in preparing the Navy fiscal year 1994 financial reports on general fund operations, \$24.6 billion of real property was counted twice.

Second, the Navy had no assurance that all plant property from only general fund activities was included in its fiscal year 1994 financial reports on general fund operations. For example, these reports excluded an indeterminable amount of plant property for as many as 290 activities or more and improperly included \$1.9 billion in plant property that belonged to 21 Navy activities engaged in the Defense Business Operations Fund (DBOF).² Neither the Navy nor the Defense Finance and Accounting Service (DFAS) compared the activities that had been included in the reports with the general fund activities listed in the Navy Comptroller Manual (now entitled, the Department of the Navy Financial Management Policy Manual). This fundamental control procedure would have detected the problems noted above.

Third, the \$291 million reported as Navy plant property work-in-progress was highly questionable. For example, some Navy and DFAS activities were not recording plant property work-in-progress transactions as required. Also, the plant property work-in-progress account balances included millions of dollars in transactions that the Navy had not promptly reviewed for transfer to plant property on-hand accounts, as required by the Navy Comptroller Manual.

Fourth, the Navy's logistics, custodial, and accounting records of real property were often not reconciled on a timely basis, or in some cases were never reconciled, which diminishes their usefulness for both accurately reporting the account balance of this property and controlling it. In one instance, for over 20 years, the Navy's financial reports overstated the real property account balance by millions of dollars because plant property at a shipyard closed in the 1970s had not been removed from the Navy's accounting records. Because this property was no longer carried in the Navy's logistic records, a reconciliation between these records and the Navy's accounting records would have identified this error.

²Navy DBOF activities include, for example, supply management, naval shipyards, naval aviation depots, naval ordnance facilities, public works centers, and research and development activities.

Background

Several organizations are integrally involved in carrying out the Navy's financial management and reporting, including: (1) the Office of the Navy's Assistant Secretary for Financial Management and Comptroller, which has overall financial responsibility, (2) DFAS, which reports to the Department of Defense (DOD) Comptroller and provides accounting and disbursing services, and (3) Navy components, which initiate and authorize financial transactions.

To help strengthen financial management, the Chief Financial Officers (CFO) Act of 1990 (Public Law 101-576) required that DOD prepare financial statements for its trust funds, revolving funds, and commercial activities, including those of the Navy. In response to experiences gained under the CFO Act, the Congress concluded that agencywide financial statements contribute to cost-effective improvements in government operations. Accordingly, when the Congress passed the Government Management Reform Act of 1994 (Public Law 103-356), it expanded the CFO Act's requirement for audited financial statements by requiring that all 24 CFO Act agencies, including DOD, annually prepare and have audited agencywide financial statements, beginning with those for fiscal year 1996.

The Government Management Reform Act authorizes the Director of the Office of Management and Budget to identify component organizations of the 24 CFO Act agencies that will also be required to prepare financial statements for their operations and have them audited. Consistent with the act's legislative history, the Office of Management and Budget has indicated that it will identify the military services as DOD components required to prepare financial statements and have them audited. Therefore, fiscal year 1996 is the first year for which the Navy will be required to prepare servicewide financial statements for its general funds.

Some Real Property Was Counted Twice

At September 30, 1994, the Navy's reported real property account balance was overstated by at least \$24.6 billion because DFAS personnel had erroneously double counted \$23.9 billion of structures and facilities and \$700 million of land. The DFAS, Cleveland Center, personnel compiling these data did not realize that the Center had received some of the same land and building accounting information from two separate sources and had incorrectly included the information from both of them in the consolidated financial reports.

To help mitigate situations such as this, in September 1995, the DFAS Director called for the DFAS center directors to take specific steps to

increase emphasis on basic internal controls. In November 1995, the DOD Comptroller clarified that DFAS and the Navy are both required to perform quality control reviews of the financial reports and statements. We believe that full and effective implementation of these directives could help to prevent future occurrences of double counting, such as the one noted during our review. For example, if the Navy and DFAS had reviewed reported financial information in that case, they would have found that real property was overstated.

Inclusion of All Plant Property From Only General Fund Activities Was Not Assured

The Navy Comptroller Manual, which governs accounting and financial policy for the Navy's plant property, classifies and lists Navy activities as involving either general fund operations or DBOF operations. The Navy and DFAS, Cleveland Center, did not have effective processes in place to ensure that all financial information on plant property from only general fund activities was included in the Navy's consolidated financial reports on general fund operations or that plant property from DBOF operations was excluded.

To compile consolidated financial reports on the Navy's general fund operations, a basic control would be to ensure that the reported figures include financial information received from all of the Navy activities identified in the manual as involving general fund operations. However, neither the Navy nor DFAS, Cleveland Center, used the listing as a control to help ensure the accuracy and completeness of the Navy's fiscal year 1994 consolidated financial reports on general fund operations.

Although the Navy Comptroller Manual needs updating, as discussed later, it was the best available information at the time of our review and listed 1,226 general fund activities at September 30, 1994. Our comparison of the list and the information used to compile the Navy's fiscal year 1994 consolidated financial reports on general fund operations showed that the reports (1) included \$34.9 billion for plant property at 936 activities that the manual listed as general fund activities but (2) did not include an indeterminable amount of plant property for the other 290 activities listed in the manual.

Also, the financial reports improperly included \$1.9 billion in plant property that belonged to 21 Navy activities engaged in DBOF operations. We identified these activities through discussions with Navy and DBOF officials. The activities had mistakenly reported to DFAS that their plant

property related to general fund operations, and neither the Navy nor DFAS, Cleveland Center, detected the error.

Navy activities engaged in general fund operations report their plant property account balances to either the Defense Accounting Office (DAO)-Norfolk or DAO-San Diego (DFAS now refers to the DAOS as operating locations). These DAOS compile the activity-level data and submit it to DFAS, Cleveland Center, which prepares both financial reports on the Navy's general fund operations and Navy DBOF financial statements.

The DAOS did not compare the listings of reporting activities with those listed in the Navy Comptroller Manual when accumulating the data. Nor did DFAS, Cleveland Center, consult the listings when consolidating the Navy's fiscal year 1994 financial reports on its general fund operations. Officials from both the Navy Comptroller's office and DFAS, Cleveland Center, told us that they had not used the listing when the fiscal year 1994 financial reports on the Navy's general fund operations were prepared because the listing was inaccurate and outdated.

Our work verified that the listing was inaccurate and outdated. We found that the reported plant property account balance included \$607 million related to 47 general fund activities that were not listed in the manual. Also, the reports included \$739 million related to 57 activities that the manual indicated were no longer operating.

Updating the manual is the joint responsibility of the Comptroller of the Navy; DFAS, Cleveland Center; and the Naval Industrial Resources Support Activity, which maintains and reports information on government furnished property. According to the Navy and DFAS, because of downsizing and consolidating of activities, updating the manual section on plant property reporting responsibilities was about a year behind schedule.

In March 1996, we recommended that the Navy and DFAS require financial information to be reviewed thoroughly to determine its reasonableness, accuracy, and completeness. When implementing this recommendation, an updated Navy Comptroller Manual listing of general fund activities could be used to review the Navy's financial reports for accuracy and completeness. In concurring with the recommendation to thoroughly review this financial information, the DOD Deputy Chief Financial Officer said that the DOD Comptroller's November 1995 clarification of the finance and accounting roles and responsibilities of DOD components and DFAS

requires a review of reported financial information. Thus, both the Navy and DFAS are now required to verify the accuracy and completeness of financial reports. Also, the September 1995 DFAS Director's guidance calls for ensuring that component reports of property, equipment, and inventory are promptly submitted and certified as to accuracy.

Reported Plant Property Work-in-Progress Account Balance Was Not Credible

The Navy's plant property account to control in-transit property and incomplete capital improvements (plant property work-in-progress) had a highly questionable \$291 million balance. We found that (1) some Navy and DFAS activities were not properly recording plant property work-in-progress transactions and (2) many Navy activities had difficulty resolving millions of dollars of in-transit property recorded in their plant property work-in-progress accounts. Consequently, these accounts were not useful in providing accurate information to ensure the prompt receipt of in-transit property or monitoring the completion of capital improvements, as intended.

The plant property work-in-progress account is designed to temporarily account for both nonmilitary equipment a Navy activity has paid for but not yet received and incomplete capital improvements to existing Navy-owned buildings. The Navy Comptroller Manual specifies that all plant property assets are to be recorded first in a work-in-progress account, with the balance then transferred to a plant property on-hand account within 2 months of in-transit property being received or 6 months of capital improvements being completed.

First, we found the following instances where the Navy and DFAS were not properly recording plant property work-in-progress transactions in accordance with the Navy Comptroller Manual's requirements.

- The Naval Sea Systems Command and the Naval Air Systems Command miscoded disbursement transactions for nonmilitary equipment purchases by 75 Navy activities. As a result, the disbursements for these assets were recorded as neither plant property work-in-progress nor nonmilitary equipment but erroneously as expenditures for consumable items.
- The plant property accounting staff at the Naval Submarine Base in Bangor, Washington, stated they were unaware of the requirement to, and thus did not, record incomplete capital improvements to existing buildings in the plant property work-in-progress account. As a result, for example, \$290,000 relating to 22 garages being added to on-base housing had not been recorded in the base's plant property work-in-progress account.

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- DAO-San Diego's computer system was not programmed to record construction on existing buildings to a Navy activity's plant property work-in-progress account. Thus, its work-in-progress account balance did not accumulate the correct data for these assets.

When situations such as these occur, the Navy's financial reports are misstated. Further, the failure to properly use plant property work-in-progress accounts essentially circumvents an internal control feature designed to help ensure that nonmilitary equipment in-transit is received and to help monitor completion of capital improvement projects.

Second, our analysis of the \$291 million plant property work-in-progress reported on the Navy's fiscal year 1994 consolidated financial reports on general fund operations showed that about 73 percent, or \$211.2 million, was related to five Navy activities. In at least the following two cases, the September 30, 1994, reported plant property work-in-progress account balances were questionable.

- The Naval Intelligence Command reported over \$84 million in plant property work-in-progress, which is (1) an increase of more than 2,000 percent from the prior year and (2) inconsistent with the \$370,000 account balance it reported for nonmilitary equipment and the \$0 balance reported for other real property.
- The Naval Criminal Investigative Service reported over \$30 million in plant property work-in-progress, which is (1) an increase of more than 165 percent over the year before and (2) inconsistent with the Service's other reported plant property—about \$400,000 in nonmilitary equipment.

We discussed with officials of these activities the questionable nature of the amounts recorded for these accounts, which could have been identified by comparing year-to-year balances. They confirmed that these account balances were incorrect and said that the activities were attempting to resolve them.

Further, our visits at other Navy activities identified additional instances where plant property work-in-progress accounts had grown substantially and resolving the large outstanding balances was a problem. Examples include the following:

- At the Fleet Combat Training Center-Atlantic, Virginia Beach, Virginia, the plant property work-in-progress account balance had been reported at about \$29 million for 2 consecutive fiscal years ending with September 30,

1993, and had increased during the following 6 months to over \$62 million. A concerted effort by the Center's civil engineering staff reduced this amount, but at September 30, 1994, over \$34 million remained in the account.

- At the Tactical Training Group-Atlantic, Virginia Beach, Virginia, the plant property official said that resolving plant property work-in-progress was a problem. For instance, a persistent effort by the Center from November 1991 to September 1993, was necessary to fully resolve \$3.5 million in transactions recorded in its plant property work-in-progress account as relating to land and buildings. The group owns no land or buildings and less than \$200,000 in nonmilitary equipment.

Plant property officials at other Navy activities—including those at the Naval Base in Norfolk, Virginia; the Naval Air Station in Millington, Tennessee; and the U.S. Naval Academy in Annapolis, Maryland—pointed to several factors contributing to problems such as these and making their resolution difficult.

They told us, for example, that DAOS assign plant property work-in-progress to Navy activities when payments are made for such items. Quarterly plant property reports to Navy activities from the DAOS show amounts for all types of plant property, including work-in-progress. To identify items to be transferred to a plant property on-hand account, the activities are to match these reports with property received and construction completed. However, the detailed supporting records needed for this comparison, such as the disbursing vouchers the DAOS prepare, are often not available at the activity level.

Also, they told us that large plant property work-in-progress account balances can result from data coding errors made by DAO disbursing personnel, causing in-transit property and incomplete construction to be recorded in the wrong activity's property records. These officials and DFAS accounting personnel said that errors can go undetected, and thus not be resolved, for years because, for instance, (1) they require a significant amount of time to identify and correct and are often given a low priority and (2) property accounting clerks lack training on resolving outstanding transactions.

Real Property Records Differed and Were Not Reconciled

The Navy and DFAS maintain separate logistical, custodial, and accounting records for real property, which comprises more than a reported \$17 billion in land, structures, and facilities. We found that information is entered separately into each of these three independently maintained sets

of records. They are often not reconciled on a timely basis or, in some instances, never reconciled, resulting in undetected and uncorrected errors and unreliable financial information.

The Naval Facilities Engineering Command (NAVFAC) maintains logistical records of real property located at all Navy activities. Because the commanding officer of each Navy activity is accountable for real property under his or her custody, each activity maintains real property custodial records. DFAS, through the DAOS, maintains the Navy's official real property accounting records.

The Navy Comptroller Manual requires Navy activities to quarterly compare their real property custodial records with (1) official Navy accounting records and (2) NAVFAC logistical records. Any errors identified through these reconciliations are to be investigated and corrected.

The Navy's consolidated financial reports on general fund operations at September 30, 1994, included \$17.2 billion as the account balance for real property. This information was prepared using the Navy's official accounting records, which included the real property for 371 Navy activities. However, as of the same date, NAVFAC's logistical records included information on 406 general fund activities reporting \$17.7 billion of real property.

To determine the reasons for this difference, we reviewed the real property records at 10 activities that, for fiscal year 1994, had a total difference of \$203 million between DFAS records and NAVFAC records. The following illustrates the types of errors identified at these activities.

- After the Boston Naval Shipyard was closed in the 1970s, NAVFAC removed the balance of the shipyard's real property accounts. However, DAO-Norfolk officials said they had not been notified of the shipyard's closing; thus, they had not removed the shipyard's \$52 million in real property from DAO records.
- According to NAVFAC records, the Naval Training Center in Bainbridge, Maryland, had \$37 million in land and buildings on-hand but under sales contract. However, Navy officials told us that this real property was excluded from the Navy's fiscal year 1994 financial reports because, before the sales contract was executed, DAO-Norfolk erroneously removed the activity from the list of reporting activities. Conversely, NAVFAC's records included \$18.9 million for Bainbridge Training Center buildings that had

been demolished. DAO and NAVFAC records were corrected when we advised officials of these errors.

- At DAO-Great Lakes, where the Navy's real property accounting records differed from NAVFAC logistic records by \$124 million at September 30, 1994, plant property accounting staff did not demonstrate a basic understanding of Navy and DFAS plant property accounting and reconciliation procedures. In one case, for example, the DFAS staff said that a Navy activity did not tell them a difference existed. In another instance, we were told that a DFAS supervisor could not find property records to support an activity's reported plant property. Rather than contact the activity, the staff stopped reporting the property.

Problems such as these are long-standing. In 1989, we recommended³ that the Navy's financial records and NAVFAC's central inventory of real property be reconciled to identify errors and help ensure accuracy. The Naval Audit Service has consistently reported similar problems in its audits of Navy DBOF financial statements under the CFO Act. For example, these audits found that the failure to reconcile Navy DBOF records and NAVFAC records resulted in a \$134 million understatement of real property in Navy DBOF fiscal year 1992 financial statements. Differences were found between these records in fiscal years 1991 and 1994 as well.

Most recently, in March 1996, we recommended that the Navy and DFAS place a high priority on implementing basic required financial controls, including reconciliations of accounts and records. The DOD Deputy Chief Financial Officer agreed with our recommendation and said that the DOD Comptroller's November 1995 guidance specifies the roles and responsibilities of DFAS and its customers with respect to reconciliations and resolution of discrepancies. Additionally, the September 1995 DFAS Director's guidance addresses DFAS's responsibility for performing reconciliations of account balances.

Conclusions

The Navy's fiscal year 1994 accounting and reporting for plant property were highly unreliable. Accurately reporting the Navy's plant property account balance is especially important to help ensure the reliability of the consolidated financial statements DOD is statutorily required to prepare, beginning with those for fiscal year 1996.

³Financial Reporting: Navy's 1986 Consolidated Report on Financial Position Is Unreliable (GAO/AFMD-89-18, April 6, 1989).

The recommendations we made in March 1996 were directed at avoiding the mistakes made in preparing the Navy's fiscal year 1994 consolidated financial reports and overarch many of the basic control weaknesses discussed in this report. These weaknesses underscore the need for the Navy and DFAS to fully and effectively implement the improvements that we recommended and that are required by the DOD Comptroller's and the DFAS Director's recent guidance. Additional specific actions are also necessary to improve plant property accounting and reporting.

Recommendations

We recommend that the Navy Assistant Secretary for Financial Management and Comptroller and the DFAS Director require that

- by September 30, 1996, the Navy Comptroller Manual provision that lists the Navy's activities engaged in general fund operations and DBOF operations be updated and accurately maintained;
- the Navy and DFAS, Cleveland Center, use this listing as one analytical procedure to help ensure that the plant property account balances reported in the Navy's financial reports are complete and include information from only general fund activities;
- Navy activities and DFAS routinely monitor plant property work-in-progress accounts and promptly review and resolve large balances;
- Navy activities promptly request, and DFAS expeditiously provide, information to assist in transferring plant property work-in-progress items to on-hand accounts and in correcting errors; and
- Navy activities and DFAS personnel be trained to identify and resolve work-in-progress and other plant property problems.

Agency Comments and Our Evaluation

In written comments on a draft of this report, DOD generally concurred with our findings and recommendations. DOD said that groups have been established to identify and resolve issues involving the consistency of report information and establish and monitor a plan of action and milestones for improving property reporting and accounting. Also, DOD said that DFAS, Cleveland, has begun a training program for the plant property staff at various DAOS.

DOD concurred with each of our recommendations and cited several planned corrective measures. For example, DOD said that improvements will be made to

- accurately maintain and periodically update information on all Navy activities that own plant property;
- develop a checklist to identify Navy and Marine Corps activities engaged in general fund operations, which will be used to help ensure that Navy reports provided to DFAS, Cleveland, are complete and include the appropriate general fund reporting activities;
- reiterate to all DFAS and Navy activities the policy on clearing work-in-progress accounts and ensure that work-in-progress information is promptly reconciled and recorded in DFAS financial records; and
- train plant property personnel, which has already begun at several DFAS locations.

DOD concurred with two of our four findings. DOD partially concurred with two of the findings because it said that references were unclear for two figures cited in our draft report: (1) the 1,226 general fund activities shown in the Navy Comptroller Manual at the time of our review and (2) the \$291 million plant property work-in-progress account balance. We provided a DFAS, Cleveland, representative with specific references in the Navy Comptroller Manual and the Navy's consolidated financial statements for fiscal year 1994 that we used as sources for these data.

Also regarding our findings, DOD said that DFAS is emphasizing the need for internal and quality controls, such as identifying Navy and Marine Corps activities engaged in general fund operations. DOD also said that it is the goal of DFAS, the Navy, and the Marine Corps to develop and implement automated and integrated system interfaces for tracking work-in-progress accounts. Further, DOD said that the Navy recognizes that it should have removed property it no longer maintained from Navy records but had failed to do so.

DOD said that most of its planned corrective actions will be accomplished within the next year and that many are planned to be completed by September 30, 1996. We believe that DOD's planned actions will fulfill the intent of our recommendations. Adhering to the projected completion schedule will help to improve the accuracy and completeness of the Navy's financial statements for general fund operations for fiscal year 1996 and subsequent fiscal years.

The full text of DOD's comments is provided in appendix II.

Our work was done as part of a broad-based review of various aspects of the Navy's financial management operations between August 1993 and February 1996 and was conducted in accordance with generally accepted government auditing standards. Our scope and methodology are discussed in appendix I and the locations where we conducted audit work are listed in appendix III.

We are sending copies of this report to the Chairmen and the Ranking Minority Members of the Senate Committee on Governmental Affairs and the House Committee on Government Reform and Oversight, as well as its Subcommittee on Government Management, Information, and Technology. We are also sending copies to the Secretary of Defense, the Secretary of the Treasury, and the Director of the Office of Management and Budget. We will make copies available to others upon request.

If you or your staffs have any questions, please contact me at (202) 512-9095. Major contributors to this report are listed in appendix IV.



Lisa G. Jacobson
Director, Defense Financial Audits

Contents

Letter	1
Appendix I Scope and Methodology	16
Appendix II Comments From the Department of Defense	18
Appendix III Locations Where Audit Work Was Conducted	24
Appendix IV Major Contributors to This Report	26

Abbreviations

CFO	Chief Financial Officers
DAO	Defense Accounting Office
DBOF	Defense Business Operations Fund
DFAS	Defense Finance and Accounting Service
DOD	Department of Defense
NAVFAC	Naval Facilities Engineering Command

Scope and Methodology

To gain an understanding of the systems and procedures used to account for and report on plant property, we reviewed applicable Navy Comptroller guidance, DOD and DFAS regulations, and instructions promulgated by Navy commands and activities. Also, we interviewed cognizant Navy, DFAS, and Treasury officials and discussed plant property management and reporting with cognizant Navy shore activity officials.

To evaluate the DFAS, Cleveland Center's, process for compiling the Navy's plant property account balance, we obtained and analyzed the detailed schedules for the fiscal years 1993 and 1994 Navy plant property account balance reported by DFAS, Cleveland Center, and its DAOS. Specifically, we

- compared the number of Navy activities reporting general fund plant property to those listed in the Navy Comptroller Manual, volume 2, chapter 5;
- compared the account balance of each reporting activity for the 2 fiscal years to identify trends or fluctuations; and
- traced the reported account balance to the supporting documentation from the DAOS.

We visited NAVFAC, Alexandria, Virginia, its Facilities Support Office in Port Hueneme, California, and its Southwest Engineering Field Division, San Diego, California, to examine how NAVFAC's central real property database (the Navy Facility Assets Data Base) works and interfaces with Navy activities and DAOS for reporting on land, facilities, and structures. We also visited the Naval Industrial Resources Support Activity in Philadelphia, Pennsylvania, to determine what property it reported to DFAS, Cleveland Center, for inclusion in the Navy's financial reports.

To analyze the amounts reported by Navy for plant property work-in-progress, we obtained the plant property amounts reported for each activity by class—land, buildings, nonmilitary equipment, and work-in-progress. We contacted seven of the activities whose plant property work-in-progress amount appeared to be incorrect when compared with its other reported plant property amounts. At the activities we visited (see appendix III), we examined property accounting procedures and compliance with Navy Comptroller requirements, such as accounting for work-in-progress, reconciliations, and physical inventories.

To compare and analyze the account balances and reporting activities among different sources of data that should agree, we obtained the consolidated financial report on general fund operations on real property

as reported to DFAS, Cleveland Center, and compared it to NAVFAC's real property logistics records.

For September 30, 1993 and 1994, we compared the detail of the reported account balances of land and facilities provided by DFAS, Cleveland Center, with those in NAVFAC's records to determine if they agreed. We did not verify the accuracy of the information in NAVFAC's database because, at the time of our work, the Naval Audit Service was reviewing the reasonableness of the database for estimating costs and savings resulting from base closure and realignment recommendations. In a February 1995 report, The Navy's Implementation of The 1995 Base Closure and Realignment Process, the Service said that the NAVFAC database was a reasonably accurate source of information for that purpose.

We requested comments on a draft of this report from the Secretary of Defense or his designee. The DOD Deputy Chief Financial Officer provided us with written comments, which are discussed in the "Agency Comments and Our Evaluation" section and reprinted in appendix II.

Comments From the Department of Defense

Note: GAO comment supplementing those in the report text appears at the end of this appendix.



COMPTROLLER

OFFICE OF THE UNDER SECRETARY OF DEFENSE
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JUN 14 1996

Mr. Gene L. Dodaro
Assistant Comptroller General
Accounting and Information Management Division
U.S. General Accounting Office
Washington, DC 20548

Dear Mr. Dodaro:

This is the Department of Defense (DoD) response to the General Accounting Office (GAO) draft report, "CFO ACT FINANCIAL AUDITS: Navy Plant Property Accounting and Reporting Is Highly Unreliable," dated April 19, 1996 (GAO Code 918842/OSD Case 1050-D).

The Department generally concurs with the subject draft report. The Defense Finance and Accounting Service (DFAS) and the Navy, cooperatively, are working to improve Navy and Marine Corps financial reporting. For example, groups have been established to review the progress being made to implement the GAO and the Naval Audit Service recommendations. These groups are identifying and attempting to resolve issues involving consistency of report information, establishing and monitoring a plan of action and milestones for improving property reporting/accounting, and ensuring that all participants are kept informed of progress and opportunities. Further, the DFAS-Cleveland Center has begun an aggressive training program with the plant property staff at various Operating Locations as a mechanism for resolving many of the items cited in the draft report.

The detailed DoD comments addressing the report findings and recommendations are provided in the enclosure.

The Department appreciates the opportunity to comment on the draft report.

Sincerely,

Alvin Tucker
Deputy Chief Financial Officer

Enclosure

DOD COMMENTS ON
GAO DRAFT AUDIT REPORT
OSD CASE 1050-D, GAO CODE 918842

“CFO ACT FINANCIAL AUDITS: NAVY PLANT PROPERTY ACCOUNTING AND
REPORTING IS HIGHLY UNRELIABLE”

FINDINGS

FINDING A: Some Real Property Was Counted Twice. The GAO found that, on September 30, 1994, the Navy reported real property account balance was overstated by at least \$24.6 billion because the Defense Finance and Accounting Service (DFAS) personnel had erroneously double-counted \$23.9 billion of structure and facilities, as well as, \$700 million of land. The GAO noted that to help mitigate such situations, the DFAS Director in September 1995 directed that specific steps be taken to increase emphasis on basic internal controls. In addition, in November 1995 the DoD Comptroller clarified that the DFAS and the Navy are both required to perform quality control reviews of the financial reports and statements. The GAO concluded that full implementation of these directives could help prevent future occurrences of double counting. (pp. 2-4/GAO Draft Report)

DOD COMMENTS: Concur. The DFAS-Cleveland Center (DFAS-CL) has taken specific steps to increase emphasis on internal controls. These improvements include assigning one accountant to each appropriation, using a CFO checklist similar to the one created by GAO, and, most importantly, reviewing and emphasizing the need for internal and quality controls with the staff. The DFAS-CL also is in the process of developing a procedure whereby the staffs, both at the DFAS-CL and its corresponding Operating Locations (OPLOCs) coordinate information received from Navy and Marine Corps activities. This internal control process is not yet complete, but, will be in place prior to the end of FY 1996.

FINDING B: Inclusion of All Plant Property From Only General Fund Activities Was Not Assured. The GAO discovered that the Navy and the DFAS, Cleveland Center, did not have effective processes in place to ensure that all financial information on plant property from only general fund activities was included in the Navy consolidated financial reports on general fund operations or that plant property from the Defense Business Operations Fund was excluded. For example, the report excluded an indeterminable amount of plant property for as many as 290 activities or more and improperly included \$1.9 billion in plant property that belonged to 21 Navy activities. (p. 2, pp. 4-5/GAO Draft Report)

Enclosure
GAO Draft Report
OSD Case 1050-D
Page 1 of 4

Appendix II
Comments From the Department of Defense

See comment 1.

DOD COMMENTS: Partially Concur. The GAO reference to the 1,226 general fund activities (page 4 of the draft report) is unclear. The DFAS-CL contacted the GAO to clarify the statement, but, as of the date that this response was prepared, the DFAS had not received an answer. The DFAS-CL is in the process of developing a quality control checklist which will identify Navy and Marine Corps activities engaged in general fund operations. Use of the checklist will help ensure that the correct activities are included in the Navy consolidated financial reports. This checklist will be available before the end of FY 1996, in time for the CFO Statement preparation. The Navy and Marine Corps are taking complimentary actions.

FINDING C: Reported Plant Property Work-In-Process Account Balance Was Not Credible. The GAO determined that the Navy plant property account to control in-transit property and incomplete capital improvements (plant property work-in-progress) had a highly questionable \$291 million balance. The GAO found and discussed examples where (1) some Navy and DFAS activities were not properly recording plant property work-in-progress transactions, and (2) many Navy activities had difficulty resolving millions of dollars of in-transit property recorded in their plant property work-in-progress accounts. (p.2, pp. 5-8/GAO Draft Report)

See comment 1.

DOD COMMENTS: Partially Concur. Although the DFAS-CL had contacted GAO to obtain specifics regarding the \$291 million referenced in the report, as of the date that this response was prepared, the DFAS-CL had not received a reply.

During the development of the FY 1996 Navy CFO financial report, the Office of the Assistant Secretary of the Navy (Financial Management and Comptroller) in coordination with the DFAS, prepared specific data call requirements to be issued to the major claimants for subsequent reporting from each of the subordinate naval activities. Although this manual process will suffice for FY 1996 reports, it is the goal of the DFAS-CL, the Navy, and the Marine Corps to develop and implement automated, and integrated, system interfaces for tracking work in-progress accounts.

FINDING D: Real Property Records Differed and Were Not Reconciled. The GAO found that the Navy and the DFAS maintain separate logistical, custodial, and accounting records for real property, and that information is entered separately into each of these three independently maintained set of records. The records are often not reconciled on a timely basis or, in some instances, never reconciled, resulting in undetected and uncorrected errors and unreliable financial information. The GAO cited one instance where for over 20 years the Navy financial reports overstated the real property account by millions of dollars because plant property at a shipyard closed in the 1970s had not been removed from the accounting records. (p.2, pp. 8-10/GAO Draft Report)

Enclosure
GAO Draft Report
OSD Case 1050-D
Page 2 of 4

DOD COMMENTS: Concur. The Navy is responsible for maintaining accurate logistical/ custodial property records and providing appropriate financial information to the DFAS. The Navy recognizes that it should have, but failed to, remove from its property records property no longer maintained by the Navy. The DFAS is modifying the existing financial systems into one interim system for financial reporting of Navy general fund property. This modification includes the development of interfacing requirements between a unified Standard Accounting and Reporting System (STARS) for field reporting and the Defense Property Accountability System (DPAS).

RECOMMENDATIONS

RECOMMENDATION 1: The GAO recommended that the Navy Assistant Secretary for Financial Management and Comptroller and the Director, DFAS, require that by September 30, 1996, the Navy Comptroller Manual provision that lists the Navy activities engaged in General Fund operations and Defense Business Operations Fund operations be updated and accurately maintained. (p.10/GAO Draft Report)

DOD COMMENTS: Concur. The Navy has replaced the Navy Comptroller Manual with the Department of the Navy Financial Management Policy Manual. The Navy will provide periodic updates to the DFAS of Naval activities as recommended by the GAO. The DFAS-CL will maintain and publish the identities of Naval activities and their related accountable designees. The DFAS-CL is reviewing its current policy for completeness and accuracy and will coordinate with the Office of the Assistant Secretary of Navy (Financial Management and Comptroller) to ensure that all activities that own plant property are identified and published. ESTIMATED COMPLETION DATE: September 30, 1996.

RECOMMENDATION 2: The GAO recommended that the Navy Assistant Secretary for Financial Management and Comptroller and the Director, DFAS, require that the Navy and the DFAS, Cleveland Center, use the list from Recommendation 1 as one analytical procedure to help ensure that the plant property account balances reported in the Navy financial reports are complete and include information from only general fund activities. (pp.10-11/GAO Draft Report)

DOD COMMENTS: Concur. The DFAS-CL is in the process of developing a checklist that identifies Navy and Marine Corps activities engaged in general fund operations. This list will be used to better ensure that Navy reports provided to the DFAS-CL are complete and include the appropriate general fund reporting activities. ESTIMATED COMPLETION DATE: September 30, 1996.

RECOMMENDATION 3: The GAO recommended that the Navy Assistant Secretary for Financial Management and Comptroller and the Director, DFAS, require that the Navy activities

Enclosure
GAO Draft Report
OSD Case 1050-D
Page 3 of 4

Appendix II
Comments From the Department of Defense

and the DFAS routinely monitor plant property work-in-progress accounts and promptly review and resolve large balances. (p.11/GAO Draft Report)

DOD COMMENTS: Concur. The NAVCOMPT Manual, Volume 3, paragraph 36519, provides guidance on clearing the Navy and Marine Corps work-in-progress account. The DFAS-CL formally will reiterate this policy with all DFAS and Navy activities. Also, the DFAS-CL Operating Location (OPLOC) at Norfolk routinely provides, to other OPLOCs and Property Accounting Activities, a listing that highlights over-aged and current outstanding plant property charges that have not been reported on the Naval Form "Reconciliation of Plant Account" (NAVCOMPT Form 167). ESTIMATED COMPLETION DATE: July 31, 1996.

RECOMMENDATION 4: The GAO recommended that the Navy Assistant Secretary of Financial Management and Comptroller and the Director, DFAS, require that the Navy activities promptly request, and the DFAS expeditiously provide, information to assist in transferring plant property work-in-progress items to on-hand accounts and in correcting errors. (p.11/GAO Draft Report)

DOD COMMENTS: Concur. The Navy is responsible for notifying the DFAS-CL when property is completed and no longer is considered work-in-progress. Upon receipt of such notification, the DFAS-CL will ensure that the information is promptly reconciled and recorded in the financial property records. The DFAS-CL will (a) reiterate this procedure to its various financial network activities, as well as, to Navy and Marine Corps logistical activities; and (b) review the processes related to property records and ensure that corrective actions, when identified, are taken. ESTIMATED COMPLETION DATES ON ITEMS: (a) September 30, 1996; (b) September 30, 1997.

RECOMMENDATION 5: The GAO recommended that the Navy Assistant Secretary for Financial Management and Comptroller and the Director, DFAS, require that the Navy activities and the DFAS personnel be trained to identify and resolve work-in-progress and other plant property problems. (p.11/GAO Draft Report)

DOD COMMENTS: Concur. The Navy will provide appropriate training for its personnel. The plant property staff at the OPLOC in Pensacola already has provided training to the plant property personnel at the OPLOCs in Oakland and San Diego. Training also will be provided to personnel at the Charleston OPLOC in the near future. This training, in addition to the actions taken in response to the above recommendations, should resolve the issues identified by GAO. ESTIMATED COMPLETION DATE: Training is on-going, with final status by March 30, 1997.

Enclosure
GAO Draft Report
OSD Case 1050-D
Page 4 of 4

The following is GAO's comment on the Department of Defense letter dated June 14, 1996.

GAO Comment

1. A representative of DFAS, Cleveland, contacted us regarding this figure and, on May 16, 1996, we provided additional information as to its source. DFAS, Cleveland, did not indicate that further clarification was necessary.

Locations Where Audit Work Was Conducted

Department of the Navy Activities

AEGIS Training Center, Dahlgren, Virginia

Facilities Support Office, Port Hueneme, California

Fleet Combat Training Center-Atlantic, Dam Neck, Virginia Beach, Virginia

Naval Air Maintenance Training Group, Millington, Tennessee

Naval Air Station, Norfolk, Virginia

Naval Air Station, Millington, Tennessee

Naval Air Station-Oceana, Virginia Beach, Virginia

Naval Air Technical Training Center, Millington, Tennessee

Naval Amphibious Base-Little Creek, Norfolk, Virginia

Naval Base, Norfolk, Virginia

Naval Computer and Telecommunications Area Master Station-Atlantic, Norfolk, Virginia

Naval Computer and Telecommunications Area Master Station-Atlantic Detachment, Key West, Florida

Navy Experimental Diving Unit, Panama City, Florida

Naval Facilities Engineering Command, Alexandria, Virginia

Naval Facilities Engineering Command-Southwest Engineering Field Division, San Diego, California

Naval Industrial Resources Support Activity, Philadelphia, Pennsylvania

Naval Space Command, Dahlgren, Virginia

Naval Submarine Base-Bangor, Silverdale, Washington

Tactical Training Group-Atlantic, Dam Neck, Virginia Beach, Virginia

Trident Refit Facility-Bangor, Silverdale, Washington

**Appendix III
Locations Where Audit Work Was
Conducted**

United States Naval Academy, Annapolis, Maryland

**Defense Finance and
Accounting Service
Activities**

Defense Finance and Accounting Service-Cleveland Center, Cleveland,
Ohio

Defense Accounting Office, Norfolk, Virginia

Defense Accounting Office, Port Hueneme, California

Defense Accounting Office, San Diego, California

Defense Accounting Office, Arlington, Virginia

Defense Accounting Office, Pensacola, Florida

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