



Report to the Chairwoman,
Subcommittee on Military Personnel,
Committee on Armed Services, House
of Representatives

January 2020

DEPARTMENT OF DEFENSE

Actions Needed to Reduce Accounting Adjustments

GAO Highlights

Highlights of [GAO-20-96](#), a report to the Chairwoman, Subcommittee on Military Personnel, Committee on Armed Services, House of Representatives

Why GAO Did This Study

DOD remains the only major federal agency that has been unable to obtain a financial statement audit opinion. One of the contributing factors is DOD's large volume of nonroutine accounting adjustments, which are used for recording corrections or adjustments in an accounting system. This report examines accounting adjustments and their effect on the reliability of DOD's financial information, the extent to which DOD has established and implemented policies and procedures for recording accounting adjustments, and the extent to which DOD has taken actions to reduce adjustments recorded at the consolidated level.

For this report, GAO reviewed DOD and DFAS's policies and procedures, interviewed DOD officials about the adjustment process, and reviewed initiatives to reduce the number of adjustments being recorded. GAO also selected a random sample of 242 adjustments recorded at the DOD consolidated level for the fourth quarter of fiscal year 2018 to determine whether the adjustments were recorded in accordance with established policies.

What GAO Recommends

GAO is making eight recommendations to DOD, which include updating and implementing policies and procedures on recording accounting adjustments and identifying steps to reduce the need for recording adjustments across the department. DOD agreed with all eight recommendations and cited actions to address them.

View [GAO-20-96](#). For more information, contact Kristen Kociolek at (202) 512-2989 or kociolek@gao.gov.

January 2020

DEPARTMENT OF DEFENSE

Actions Needed to Reduce Accounting Adjustments

What GAO Found

While the use of accounting adjustments is a common practice, the Department of Defense's (DOD) reliance on a large volume of nonroutine adjustments to prepare its financial statements is primarily a result of deficient business processes and limitations in accounting systems that DOD components use to process financial information. For example, the Defense Finance and Accounting Service (DFAS) continues to rely on forced-balance adjustments to replace the financial information that DOD's components submit to force agreement with Department of the Treasury balances without reconciling and researching the cause of differences (see figure). The recording of these adjustments was identified as a material weakness in DOD's internal control over financial reporting in its fiscal year 2018 financial statement audit.

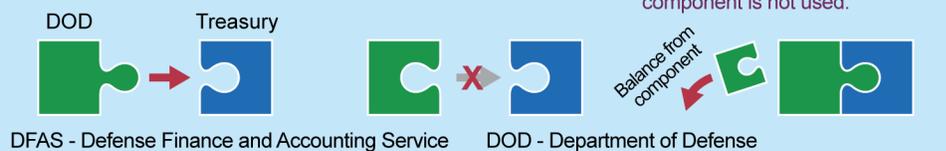
Forced-Balance Adjustment Process

Forced-balance adjustments are made outside of the routine course of business, without adequate supporting documentation, and are referred to as plugs. The Department of the Treasury (Treasury) requires that agencies perform a monthly "book to bank" reconciliation, much like individuals would balance their checkbooks.

A "fund balance" recorded by DOD should match the balance recorded by Treasury.

When the balances do not match, the difference must be reconciled.

DFAS records a forced-balance adjustment, or a "plug," so the two balances will match. The balance submitted by a DOD component is not used.



Source: GAO analysis of GAO and DOD information. | GAO 20-96

GAO found that DOD and DFAS policies and procedures for accounting adjustments are insufficient, outdated, and inconsistently implemented. For example, DOD's current policies do not define what constitutes adequate supporting documentation for system-generated adjustments, nor have DOD and DFAS established policies for identifying the cause of the adjustments, developing and implementing action plans to reduce the need for adjustments, and monitoring the effectiveness of those action plans. Because DOD and DFAS are not ensuring that their policies and procedures are up-to-date and consistently implemented, there is an increased risk that inaccurate, invalid, or unapproved adjustments will be recorded in DOD's core financial reporting system, resulting in a misstatement in DOD's consolidated financial statements.

DOD and DFAS have undertaken initiatives to address some of the issues that contribute to the need for adjustments. Both organizations have developed strategies to decrease adjustments; however, neither has developed specific outcomes or detailed procedures for achieving stated goals in the strategies. Without clear procedures on how to implement its initiatives and a complete understanding across DOD of the issues contributing to the need for accounting adjustments, there is an increased risk that management efforts to reduce adjustments at the DOD consolidated level will be inefficient and ineffective.

Contents

Letter		1
	Background	4
	Some Types of Adjustments That DOD Routinely Records Indicate Critical Weaknesses in DOD's Processes and Affect the Reliability of Its Financial Information	9
	DOD and DFAS Policies and Procedures for Recording Accounting Adjustments Are Inadequate and Inconsistently Followed	14
	DOD and DFAS Have Taken Actions to Reduce Accounting Adjustments but Lack Procedures for Implementing a Department-Wide Strategy	29
	Conclusions	32
	Recommendations for Executive Action	33
	Agency Comments and Our Evaluation	34
Appendix I	Objectives, Scope, and Methodology	35
Appendix II	Comments from the Department of Defense	39
Appendix III	GAO Contact and Staff Acknowledgments	42
Table		
	Table 1: Selected Accounting Adjustments Sample	37
Figures		
	Figure 1: Recording of the Department of Defense (DOD) Accounting Transactions	5
	Figure 2: The Department of Defense's (DOD) Consolidation Process	6
	Figure 3: Where Accounting Adjustments Can Be Recorded during the Department of Defense (DOD) Consolidated Process	8
	Figure 4: Forced-Balance Adjustment Process	11
	Figure 5: Identification and Analysis of Root Cause and the Implementation and Monitoring of Action Plans for Accounting Adjustments	24

Figure 6: Inconsistency of Information in White Papers between DFAS Sites	26
Figure 7: Inconsistency of Information in White Papers within a DFAS Site	27

Abbreviations

Business Plan	<i>Fiscal Year 2018 Annual Business Plan</i>
DDRS	Defense Departmental Reporting System
DDRS-AFS	Defense Departmental Reporting System—Audited Financial Statements
DDRS-B	Defense Departmental Reporting System—Budgetary
DFAS	Defense Finance and Accounting Service
DOD	Department of Defense
ERP	enterprise resource planning
FBWT	Fund Balance with Treasury
FECA	Federal Employees’ Compensation Act
FMR	Financial Management Regulation
JV	journal voucher
OIG	Office of Inspector General
OUSD	Office of the Under Secretary of Defense
Strategy	<i>DOD Financial Management Strategy Fiscal Years 2016–2020</i>
Strategic Plan	<i>Fiscal Years 2017–2021 Strategic Plan</i>
Treasury	Department of the Treasury
USSGL	<i>U.S. Standard General Ledger</i>

This is a work of the U.S. government and is not subject to copyright protection in the United States. The published product may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.



January 10, 2020

The Honorable Jackie Speier
Chairwoman
Subcommittee on Military Personnel
Committee on Armed Services
House of Representatives

Dear Madam Chairwoman:

The Department of Defense (DOD) is responsible for about half of the federal government's discretionary spending, yet it remains the only major federal agency that has been unable to receive an audit opinion of any kind on its department-wide financial statements.¹ Since 1995, GAO has designated DOD financial management as high risk because of pervasive weaknesses in its financial management systems, business processes, internal controls, and financial reporting.² These weaknesses have adversely affected DOD's ability to prepare auditable financial statements, which is one of three major impediments preventing us from expressing an opinion on the U.S. government's consolidated financial statements.³

The National Defense Authorization Act for Fiscal Year 2014 required the Secretary of Defense to ensure that a full audit was performed on DOD's fiscal year 2018 financial statements and to submit the results to

¹Discretionary spending refers to outlays from budget authority that are provided in and controlled by appropriation acts, unlike mandatory spending, such as Medicare and other entitlement programs. For fiscal year 2018, DOD's discretionary budget authority of \$695 billion constituted about 49 percent of the total discretionary budget authority of the federal government.

²GAO, *High-Risk Series: Substantial Efforts Needed to Achieve Greater Progress on High-Risk Areas*, [GAO-19-157SP](#) (Washington, D.C.: Mar. 6, 2019).

³The other two impediments preventing us from rendering an opinion on the federal government's consolidated financial statements are (1) the federal government's inability to adequately account for and reconcile intragovernmental activity and balances between federal entities and (2) the federal government's ineffective process for preparing the consolidated financial statements. See GAO, *Financial Audit: Fiscal Years 2018 and 2017 Consolidated Financial Statements of the U.S. Government*, [GAO-19-294R](#) (Washington, D.C.: Mar. 28, 2019).

Congress no later than March 31, 2019.⁴ In fiscal year 2018, DOD underwent a full audit of its financial statements, which resulted in a disclaimer of opinion⁵ and the identification of 20 material weaknesses in internal control over financial reporting.⁶ One of the material weaknesses auditors identified related to accounting adjustments.⁷

Accounting adjustments are entries for recording corrections or adjustments in an accounting system. While the use of adjustments is common practice, DOD's reliance on a large volume of nonroutine adjustments to prepare its financial statements is primarily a result of deficient business processes. First highlighted by auditors as a material weakness in fiscal year 2005, DOD's widespread use of accounting adjustments continues to affect the reliability of its financial information at both component and department-wide levels.⁸ DOD management reported in its fiscal year 2018 agency financial report⁹ that DOD's (1) continuing inability to reconcile detail-level transactions within their general ledgers, (2) lack of adequate supporting documentation for accounting adjustments, and (3) inconsistent procedures for recording accounting adjustments constitute a material weakness in internal control

⁴Pub. L. No. 113-66, div. A, § 1003, 127 Stat. 672, 842 (Dec. 26, 2013). This provision was repealed by the National Defense Authorization Act for Fiscal Year 2018, Pub. L. No. 115-91, div. A, § 1002(b), 131 Stat. 1283, 1538 (Dec. 12, 2017), which instead enacted a permanent requirement for annual DOD financial statement audits, now codified as section 240a of Title 10, *United States Code*.

⁵A disclaimer of opinion arises when the auditor is unable to obtain sufficient, appropriate audit evidence to provide a basis for an audit opinion and accordingly does not express an opinion on the financial statements.

⁶A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.

⁷Accounting adjustments are often referred to as journal vouchers, or JVs.

⁸DOD components are subsidiary organizations within DOD and include the following: Office of Secretary of Defense; the Chairman, Joint Chiefs of Staff and the Joint Staff; the DOD Inspector General; the Military Departments (Army, Air Force, and Navy); the Defense Agencies; DOD Field Activities; the Combatant Commands; the Uniformed Services University of the Health Sciences, and all nonappropriated fund instrumentalities.

⁹Department of Defense, *Department of Defense Agency Financial Report Fiscal Year 2018* (Washington, D.C.: 2018).

over financial reporting.¹⁰ Until DOD takes steps to address these deficiencies, DOD management and Congress will not be able to rely on financial information in the agency's core financial reporting system for obtaining reliable and accurate financial information to support its decision-making.¹¹

You requested that we review DOD's accounting adjustments recorded at the consolidated financial statement level and determine the causes of these adjustments. This report examines (1) accounting adjustments and their effect on the reliability of DOD's financial information, (2) the extent to which DOD has established and implemented policies and procedures for recording accounting adjustments, and (3) the extent to which DOD has taken actions to reduce accounting adjustments recorded at the consolidated level.

To address our first objective, we reviewed DOD and Defense Finance and Accounting Service (DFAS) policies and procedures related to accounting adjustments, performed walk-throughs of DFAS's accounting adjustment process, and interviewed agency officials to gain an understanding of the processes and related controls for recording accounting adjustments at the consolidated level. Additionally, we obtained and analyzed information for fiscal years 2017 through 2018 for various types of accounting adjustments.

To address our second objective, we reviewed DOD and DFAS policies and procedures and interviewed officials from DFAS and the Office of the Under Secretary of Defense (OUSD) (Comptroller) to identify issues surrounding accounting adjustments and the procedures used to process, review, and approve these adjustments in DOD systems. We also inquired about the procedures used to determine the underlying causes of accounting adjustments, if action plans to address the causes have been developed, and the status of these plans and assessed whether the

¹⁰A general ledger is a record of all the accounts that an organization uses to record financial transactions.

¹¹DOD uses the Defense Departmental Reporting System (DDRS) for financial reporting purposes. DDRS has several modules, three of which are DDRS-Budgetary (DDRS-B), DDRS—Audited Financial Statements (DDRS-AFS), and DDRS—AFS Beginning Balance Adjustments. DDRS-B accepts summary-level information from field-level accounting systems (accounting systems that DOD components use) and ensures that they follow the standard format for government reporting. The Defense Finance and Accounting Service use DDRS-AFS and DDRS-AFS Beginning Balance Adjustments in preparing the consolidated financial statements.

implemented action plans are monitored for effectiveness. Additionally, we performed tests of controls on a random sample of 242 accounting adjustments from a population of 200,468 adjustments recorded at the consolidated level that impacted the fourth quarter of fiscal year 2018. The adjustments selected for testing were recorded in DOD's core financial reporting system. Specifically, we selected a random sample of 225 adjustments recorded in Defense Departmental Reporting System (DDRS)-Budgetary (DDRS-B) and DDRS-Audited Financial Statements (AFS) and all 17 adjustments recorded in the DDRS-AFS Beginning Balance Adjustments. We were able to project the results of testing the randomly selected sample to the population of accounting adjustments.¹² We reviewed documentation to determine whether the adjustments were properly supported in accordance with DOD policies.

To address our third objective, we reviewed documentation and interviewed DFAS and OUSD (Comptroller) officials to identify DOD and DFAS initiatives aimed at reducing the use of accounting adjustments and the procedures in place for implementing these initiatives. Further details on our scope and methodology are provided in appendix I.

We conducted this performance audit from November 2018 to January 2020 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

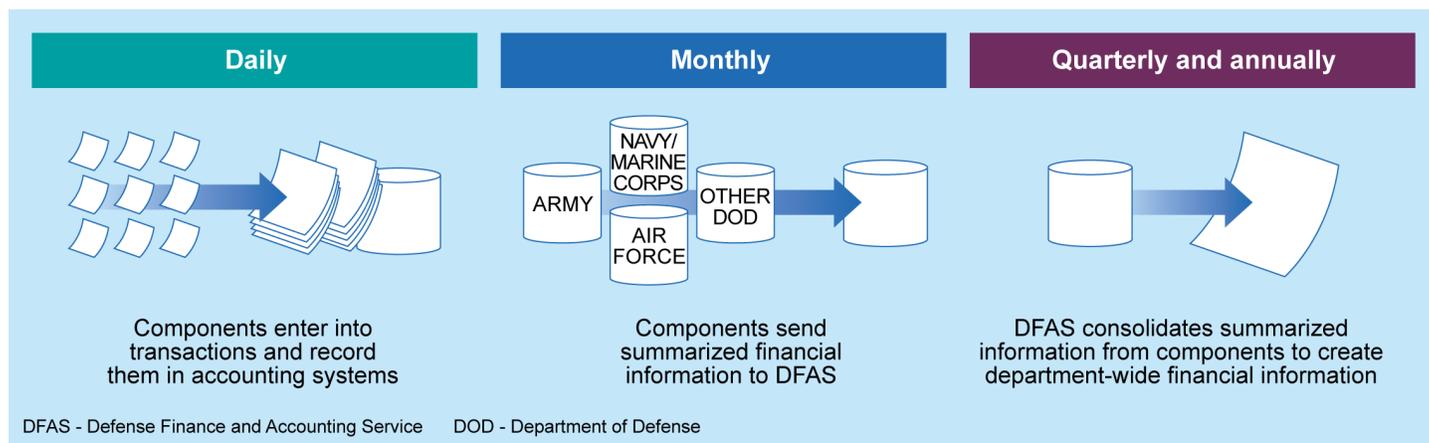
To ensure sound management and long-term stability in their operations, organizations track their financial activities (transactions), such as expenses they incur and income they generate. Organizations record their daily transactions, which increase or decrease account balances, in their accounting systems. For example, an organization's "cash balance" account increases when customers make payments due for goods or

¹²We designed the sample to support estimation for all supported accounting adjustments with a margin of error no greater than plus or minus 11.7 percentage points at the 95 percent level of confidence. For all unsupported accounting adjustments we used a margin of error no greater than plus or minus 11.8 percentage points at the 95 percent level of confidence and estimation overall for all accounting adjustments with a margin of error no greater than plus or minus 8.4 percentage points at the 95 percent level of confidence.

services previously provided, while other account balances, such as “accounts receivable” (the amount owed to an organization for goods or services provided), decrease because customers are paying part of what they owed to the organization.

At DOD, as seen in figure 1, this daily process of recording transactions in accounting systems occurs at individual DOD components. These components use multiple accounting systems to record and summarize their financial transactions.¹³ Each month, quarter, and year, components send summarized financial information to DFAS, the DOD agency that provides accounting support for DOD.¹⁴ DOD’s core financial reporting system consolidates the summarized financial information from individual components into DOD’s department-wide financial information.¹⁵

Figure 1: Recording of the Department of Defense (DOD) Accounting Transactions



Source: GAO analysis of DOD information. | GAO-20-96

¹³Most components have several accounting systems that capture accounting information. For example, the General Fund Enterprise Business System is the Army’s primary accounting system used to record the majority of the Army’s transactions.

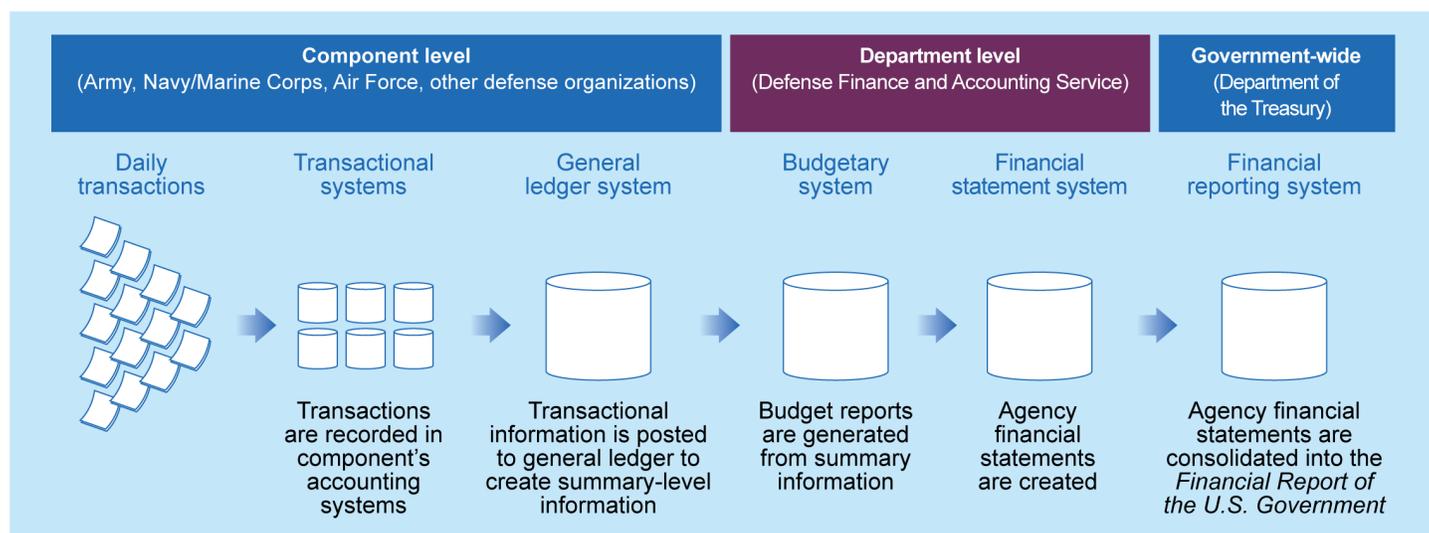
¹⁴There are three DFAS sites located in Cleveland, Ohio; Columbus, Ohio; and Indianapolis, Indiana. DFAS Cleveland supports the Navy and Marine Corps, whereas DFAS Columbus supports the Air Force. DFAS Indianapolis provides most of the Army’s accounting support, but DFAS Columbus also provides a small portion.

¹⁵The one exception at DOD is the U.S. Army Corps of Engineers, which prepares its own financial statements without DFAS assistance and submits its financial information for DOD consolidation purposes.

Financial statements provide information about an organization’s financial position—such as assets (what it owns) and liabilities (what it owes)—as of a certain point in time, in addition to the financial results of its operations—such as revenue (what came in) and expenses (what went out)—over a period of time, such as a fiscal year. Financial statements are prepared based on the summarized, or consolidated, financial information from an organization’s accounting systems. Their reliability depends on there being accurate financial information in the accounting systems.

Federal agencies such as DOD combine summarized financial information from their subsidiary organizations (e.g., DOD’s military components—Army, Air Force, Navy, and Marine Corps) to produce consolidated financial statements, as seen in figure 2. Agency management takes steps to ensure that the financial information contained in financial statements is reliable and accurate. Federal agencies submit their financial information to the Department of the Treasury (Treasury), which then combines the information for presentation in the consolidated financial statements of the U.S. government. Reliable and complete financial information is necessary to help agency management and Congress understand the agency’s finances, make informed policy and resource decisions, and hold agency officials accountable for their use of these resources.

Figure 2: The Department of Defense’s (DOD) Consolidation Process



Source: GAO analysis of DOD information. | GAO-20-96

The Role of Accounting Adjustments in the Financial Statement Process

Accounting adjustments are used to record corrections or adjustments to transactions in an accounting system. They are usually prepared at the end of an accounting period to adjust ending account balances. For example, accounting adjustments can be recorded monthly, quarterly, or annually to

- record or accrue an activity that is not accounted for in the organization's accounting systems, such as certain payroll expenses;¹⁶
- correct errors identified in processing financial information;
- record transactions based on the result of reconciliations;¹⁷
- record additional information at the request of a subsidiary organization; or
- record necessary accounting adjustments caused by accounting system limitations or timing differences.

Organizations often record such accounting adjustments when preparing financial statements. For example, adjustments to eliminate intragovernmental transactions, such as accounts receivable and sales, may be recorded.¹⁸ These adjustments are particularly necessary to consolidate information from subsidiary organizations and properly present consolidated financial statements.

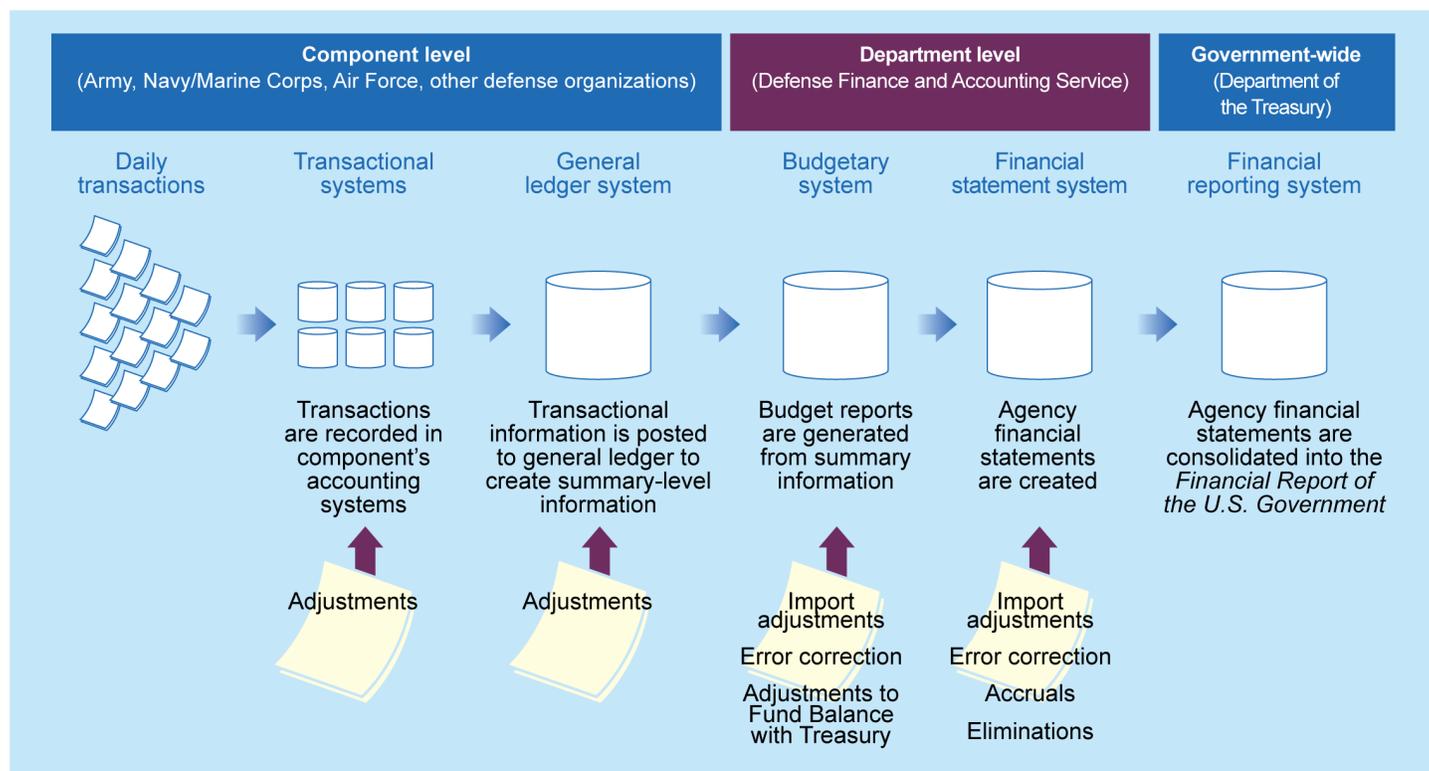
¹⁶Accrue means to make provision for an asset or liability at the end of a financial period for an event or a transaction that has taken place but is not yet recorded, for example, because it has not yet been invoiced. For example, if the end of an accounting period falls between an organization's pay periods, the organization needs to record a payroll liability for the days employees have worked but not yet been paid and include this accrued liability in its financial statements.

¹⁷Reconciliation consists of comparing two or more sets of records, researching and resolving any differences, and recording adjustments if necessary. Reconciliations are to be performed routinely so that any problems are detected and corrected promptly and differences are not allowed to age thereby becoming increasingly difficult to research.

¹⁸Intragovernmental transactions pertain to activities and balances that take place between components of a federal agency or with another federal agency. For example, when one federal agency sells goods to another, the seller records in its accounting system the amount the buyer owes to the seller. This amount is known as an account receivable to the seller and an account payable for the buyer. During the consolidation process, both the account receivable and account payable are eliminated to avoid overstating the intragovernmental accounts.

At DOD, components record accounting adjustments within their own accounting systems, and DFAS records adjustments at the consolidated level in DOD's core financial reporting system.¹⁹ DFAS often has to reformat the summary information it receives from the components' accounting systems before DOD's core financial reporting system can accept and process it. To address these or other issues in the financial information it receives as part of the consolidation process, DFAS records accounting adjustments. See figure 3 for an example of where accounting adjustments can be recorded during the consolidation process.

Figure 3: Where Accounting Adjustments Can Be Recorded during the Department of Defense (DOD) Consolidation Process



Source: GAO analysis of DOD information. | GAO-20-96

¹⁹In addition to DFAS staff, some non-DFAS staff, such as staff in DOD's Washington Headquarters Services and the U.S. Army Corps of Engineers, have the capability to record adjustments directly into DOD's core financial reporting system.

DFAS records accounting adjustments both manually and automatically in an accounting system. DFAS personnel record manual adjustments to (1) adjust errors identified during the financial statement compilation process, (2) record necessary accounting adjustments caused by system limitations or timing differences, and (3) prepare required month-end and year-end closing adjustments. System-generated adjustments are automatically recorded in the accounting system without manual involvement. DFAS uses system-generated adjustments when the volume of adjustments needed for a particular purpose is too high and labor-intensive for the adjustments to be recorded manually. For the fourth quarter of fiscal year 2018, DFAS processed 18,521 manual and 181,947 system-generated adjustments at the consolidated level.

Some Types of Adjustments That DOD Routinely Records Indicate Critical Weaknesses in DOD's Processes and Affect the Reliability of Its Financial Information

During the fourth quarter of fiscal year 2018, as noted above, DFAS recorded, at a DOD consolidated level, over 200,000 accounting adjustments in DOD's core financial reporting system. The large volume of these adjustments is one of the major impediments to DOD maintaining accurate and reliable financial information. While some of these adjustments are expected in the routine course of business, others—such as those DOD records to force account balances to match—are not.

We found that DFAS's lack of reliable business processes and limitations in the source-level accounting systems that DOD components use to process financial information leads them to record adjustments to remove and replace component-submitted financial information in order to force account balances to agree with Treasury balances. The recording of these types of adjustments was identified as a material weakness in DOD's internal control over financial reporting in its fiscal year 2019 financial statement audit. While DOD has taken steps to address this issue, because of the multitude of contributing factors involved, DOD faces significant challenges in its effort to successfully reconcile its account balances with Treasury and eliminate the need for recording these adjustments.

Some Adjustments Are Expected and Routine, While Others Are Not

Some manual and system-generated accounting adjustments are expected in the routine course of business and are recurring in nature. For example, elimination adjustments for intragovernmental balances, as previously discussed, are necessary in order to avoid overstating the account balances of subsidiary organizations in the consolidated financial information. The need for these types of adjustments occurs on a regular basis when two or more DOD components enter into business

transactions with each other. For example, when the Army purchases weapons from the Defense Logistics Agency, the Army records the transaction as an expense while the Defense Logistics Agency records this transaction as revenue in its accounting system. At the DOD consolidated level, both the revenue and expense reported at the subsidiary level need to be eliminated to avoid overstating revenue and expense for DOD as a whole. These elimination adjustments are routine, expected, and recurring because they must be prepared every time DFAS compiles DOD's quarterly and annual consolidated financial statements.

Other adjustments, such as those DFAS records in order to force account balances to match (forced-balance adjustments) are not expected within the routine course of business. DOD defines a forced-balance adjustment as any amount recorded, usually at a summary level, to eliminate differences between the component's general ledger balance and Treasury's control total. Such adjustments, recorded without adequate supporting documentation at the transaction level, are commonly referred to by the accounting community as plugs.

Fund Balance with Treasury (FBWT) adjustments are one example of forced-balance adjustments DFAS records to eliminate differences between its cash balances and the amounts Treasury reported.²⁰ In the federal government, Treasury acts as the government's bank and keeps an official record of the remaining spending authority for each agency. Consequently, reconciling an agency's FBWT account with Treasury-reported amounts is similar to an individual reconciling a checkbook to a bank statement. Treasury requires agencies to reconcile their cash balances each month with the balances reported in Treasury's records.²¹ However, DOD generally records adjustments to make its FBWT agree

²⁰The FBWT is an asset account that shows the available budget authority of federal agencies. Collections and disbursements by agencies increase or decrease the balance in the account. Agencies report changes in this account to Treasury through monthly reporting. To ensure the integrity of the collection and disbursement information that agencies submit, Treasury's Bureau of the Fiscal Service compares agencies' fund balance reporting with comparable information from financial institutions and Treasury Regional Financial Centers. Agencies are notified of any discrepancies on a monthly Statement of Differences report. Agencies are responsible for investigating and resolving these differences and reporting any required adjustments in their monthly reports. In addition to FBWT accounts, certain entities may have direct deposit authority with Federal Reserve Banks or with private sector financial institutions.

²¹The *Treasury Financial Manual* requires agencies to reconcile their FBWT accounts to Treasury balances each month; see DOD 7000.14-R, *Financial Management Regulation*, Volume 4, ch.1: *Financial Control of Assets* (January 2016).

with Treasury's records rather than performing proper research to identify what caused the differences. (See fig. 4 for more information on forced-balance adjustments.)

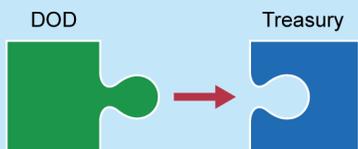
Figure 4: Forced-Balance Adjustment Process

Forced-balance adjustments are made outside of the routine course of business, without adequate supporting documentation, and are referred to as plugs. The Department of the Treasury (Treasury) requires that agencies perform a monthly "book to bank" reconciliation, much like individuals would balance their checkbooks.

A "fund balance" recorded by the Department of Defense (DOD) should match the balance recorded by Treasury.

When the balances do not match, the difference must be reconciled.

The Defense Finance and Accounting Service (DFAS) records a forced-balance adjustment, or a "plug," so the two balances will match. The balance submitted by a DOD component is not used.



Source: GAO analysis of GAO and DOD information. | GAO 20-96

DOD's Use of Certain Forced-Balance Adjustments May Indicate Critical Weaknesses

The use of forced-balance accounting adjustments affects the reliability of an organization's financial information and may indicate weaknesses within its systems and processes. Over the years, DOD's practice of recording forced-balance adjustments has been questioned by GAO and by DOD's auditors.²² For example, in an audit of the Army General Fund's reconciliation process for the FBWT account, DOD's Office of Inspector General (OIG) stated that the Army and personnel in DFAS's Indianapolis office "make forced-balance adjustments, which are unsupported manual and system-generated adjustments."²³ GAO and an independent accounting firm both reported similar practices at the Navy and Marine Corps.²⁴ These audits have repeatedly identified limitations within the

²²These include public accounting firms and DOD's Office of Inspector General.

²³Department of Defense, Office of Inspector General, *Ineffective Fund Balance with Treasury Reconciliation Process for Army General Fund*, DODIG-2017-069 (Mar. 23, 2017).

²⁴GAO, *DOD Financial Management: Ongoing Challenges with Reconciling Navy and Marine Corps Fund Balance with Treasury*, GAO-12-132 (Washington, D.C.: Dec. 20, 2011). Ernst & Young, *Department of the Navy, Notice of Finding and Recommendation, Period Ended September 30, 2018*, Ref. Number 2018-0007-FIN-GF (Aug. 30, 2018).

source-level accounting systems that DOD components use and the multitude of legacy systems (computer systems that are outdated or that can no longer receive support and maintenance but are still essential for an organization) as the main contributing factors for the use of forced-balance adjustments.

DOD's Financial Management Regulation (FMR) states that a forced-balance adjustment does not represent an adequate reconciliation. Instead, DOD components are required to maintain detailed reconciliation documentation to provide an adequate audit trail.²⁵ Further, according to the FMR, a reconciliation is not complete until all differences are identified, accountability is assigned, differences are explained, and appropriate adjustments are made to records.²⁶ These activities are needed to establish an adequate audit trail. Despite this policy, during the fourth quarter of fiscal year 2018, we found that DFAS recorded approximately 36,000, or over 17 percent of the total accounting adjustments, to force the FBWT accounts to agree with Treasury. Out of the 242 fiscal year 2018 fourth quarter accounting adjustments we selected for testing, nine were FBWT forced-balance accounting adjustments related to undistributed collections and disbursements.

Based on our review of these adjustments, we found that DFAS continues to rely on forced-balance adjustments to correct the differences between amounts DOD recorded and those that Treasury reported without properly investigating and resolving the differences. Specifically, we found that DFAS systematically recorded forced-balance adjustments to replace information that DOD components submitted with the amounts that Treasury reported without reconciling and researching the causes of differences and making any appropriate adjustments. DFAS indicated that it performs reconciliations on the FBWT accounts when compiling financial statements and researches the causes of any differences arising from these reconciliations after it records the forced-balance adjustments. However, for our sample of nine FBWT forced-balance adjustments related to undistributed collections and disbursements, DFAS was unable to provide evidence that these reconciliations were performed or that the causes of differences were researched or resolved. Rather, DFAS

²⁵DOD FMR, vol. 4, ch. 2, *Accounting for Cash and Fund Balance with Treasury*, pp. 2-9, 2-18, and 2-25 (January 2016).

²⁶DOD FMR, vol. 4, ch. 2, pp. 2-8.

provided a general description of the reconciliation process it expects each of the three DFAS sites to perform.

DOD Has Started Addressing FBWT Issues, but Many Challenges Remain

According to DOD officials, DOD has identified some key causes of the long-standing challenges in reconciling its account balances with Treasury. As noted above, many of these challenges are caused by timing issues, limitations in the source-level accounting systems that DOD components use, or the multitude of legacy systems that different DOD components use. To address these challenges, DOD is currently implementing enterprise resource planning (ERP) systems in the military services,²⁷ such as the Defense Enterprise Accounting and Management System that the Air Force uses.²⁸ These systems will replace the current legacy systems across DOD with the expectation of a full transition to ERP systems at all military services by 2025, at which point DOD expects the need to record forced-balance adjustments to decrease. OUSD (Comptroller) has a plan for implementing ERP systems at smaller DOD components that also use legacy systems. However, the challenges that legacy systems cause are likely to continue until the ERP transitions are completed and ERP systems are fully implemented at the military services and smaller DOD components. A DFAS official stated that until DOD fully implements the ERP systems, DFAS does not have any plans to modify the current financial management environment to eliminate the recording of these types of adjustments. As noted earlier, as part of the routine course of business certain adjustments will still need to be made following the full implementation of the ERP systems.

Along with DOD's implementing of the ERP systems, DOD officials stated that some DFAS sites, in coordination with various DOD components, have implemented tools to help them reconcile FBWT balances and research the causes of any differences arising during these reconciliations.²⁹ According to DOD officials, these tools have the ability

²⁷Enterprise resource planning refers to a type of software that organizations use to manage day-to-day business activities, such as accounting, procurement, project management, risk management and compliance, and supply chain management.

²⁸According to Air Force officials, the Air Force will use the Defense Enterprise Accounting and Management System as the accounting system for all new activity starting in fiscal year 2020. However, because appropriations accounts generally remain open for 5 years after their expiration to liquidate properly made obligations, the current legacy general ledger system—General Accounting and Finance System-Reengineered—will continue to have activity until fiscal year 2025.

²⁹These tools include the Army and Navy FBWT tools.

to produce supporting documentation for management and auditors to use when reviewing FBWT accounts. However, DFAS did not provide supporting documentation for these reconciliations in order for us to verify that they had been performed. Until DOD consistently performs and documents the required reconciliations to identify the causes for these types of adjustments and takes a holistic approach to resolving them, DOD's financial management issues—such as those associated with FBWT—are likely to continue, resulting in a continued inability to produce reliable and auditable consolidated financial statements.

DOD and DFAS Policies and Procedures for Recording Accounting Adjustments Are Inadequate and Inconsistently Followed

Establishing clear policies and procedures for recording accounting adjustments is crucial for (1) ensuring that accounting adjustments are properly recorded and adequately supported with documentation; (2) identifying the underlying causes for the recording of adjustments; and (3) developing, implementing, and monitoring action plans to reduce the need for accounting adjustments. We found that DOD and DFAS policies and procedures for recording accounting adjustments were insufficient, outdated, and not consistently implemented. Additionally, we found that DOD and DFAS lacked policies and procedures in certain key areas, such as performing cause analyses and developing action plans to reduce the need for accounting adjustments. By not ensuring that policies and procedures are up-to-date and consistently implemented, DOD faces an increased risk that inaccurate, invalid, or unapproved adjustments will be recorded in its core financial reporting system, resulting in misstatements in its consolidated financial statements.

Policies and Procedures for Maintaining Adequate Supporting Documentation for System-Generated Accounting Adjustments Are Insufficient

System-generated accounting adjustments are recorded automatically in an accounting system and have unique characteristics and processes that differ from those applicable to manual accounting adjustments. Unlike manual adjustments, which are initiated, recorded, and approved in the accounting system by a person, system-generated adjustments are guided by business rules embedded in an accounting system. These business rules drive the accounting adjustment process and are configured to record the adjustment when certain conditions are met. We found that DFAS lacked documentation to support the business rules, such as documentation of programming logic that creates the system-generated adjustments.

Based on our review of accounting adjustments at DOD, we found that system-generated adjustments are recorded in large numbers and account for the majority of the accounting adjustments that DFAS

recorded. For example, for the fourth quarter of fiscal year 2018, system-generated accounting adjustments accounted for over 90 percent of the total volume of adjustments recorded in DOD's core financial reporting system at the consolidated level. Given the magnitude and unique characteristics of system-generated adjustments, developing and maintaining adequate supporting documentation are critical. According to the FMR, adjustments to the accounting records should be supported with sufficiently detailed written documentation to provide an audit trail to the source transaction that requires the adjustment. Further, the FMR requires supporting documentation to include information such as the reason for the adjustment, calculation of the adjustment amount, and evidence of managerial review and approval of the adjustment.

To support certain types of recurring system-generated adjustments, DFAS developed eight standardized narratives that include the reasons for the adjustments and the documentation DFAS considers necessary to support the adjustments.³⁰ Other recurring system-generated adjustments are recorded based on System Change Requests, which are proposals to modify information in an accounting system such as revising programming logic and coding changes.³¹ In the fourth quarter of fiscal year 2018, DOD determined that 74 percent of the recorded system-generated adjustments related to four of the eight standardized narratives. Most of the System Change Requests we tested related to financial information migration from a legacy system to a new responsible work area for the U.S. Army Corps of Engineers.

DFAS annually selects and reviews a random sample of 40 system-generated adjustments related to each type of narrative for which supporting packages are prepared. According to DFAS officials, the supporting package preparation for the selected sample involves verifying

³⁰The eight narratives for fiscal year 2018 were Extended Appropriations, Flow-back Adjustments, Funding Adjustments, Pre-close Canceling Appropriations, Reapportionment, Reversal, Army Undistributed Adjustments, and Navy Undistributed Adjustments. The narratives document the internal controls over these types of adjustments. Four of the eight types were selected in our testing sample: Funding Adjustments, Pre-close Canceling Appropriations, and both Army and Navy Undistributed Adjustments.

³¹According to DFAS officials, the bulk of System Change Requests processed in the fourth quarter of fiscal year 2018 were not related to system-generated adjustments.

that the adjustments impacted the intended accounts.³² If no issues are identified, DFAS concludes that the core financial reporting system recorded the adjustments as intended, the desired results were achieved, and the adjustments were supported. Within a given year, if DFAS sample testing demonstrates that a certain type of system-generated adjustment was supported, DFAS categorizes all the accounting adjustments that relate to this particular type as supported for the rest of the year.

We found that other than the supporting packages created specifically for the periodic random samples, DFAS maintains no other documentation to support the system-generated adjustments related to each of the eight narratives. As part of our audit, we selected for testing 242 accounting adjustments that impacted the financial statements for the fourth quarter of fiscal year 2018, of which 93 were system-generated accounting adjustments. Of these 93 adjustments, DFAS categorized 42 as unsupported and 51 as supported. DFAS categorized adjustments as either supported or unsupported depending upon the circumstances. The circumstances considered include whether it relates to one of the eight narratives or to specific System Change Requests. When the eight narratives are tested, if no issues are identified as part of the testing, the transactions linked to that narrative are considered supported.³³ However, we determined that the corresponding narratives and System Change Requests were insufficient support for the 51 adjustments categorized as supported because we were unable to verify the validity and accuracy of the adjustments with supporting documentation.

In addition, we found that DFAS did not maintain evidence demonstrating the review and approval of the programming of predefined business rules in the systems that recorded the adjustments. When our results are projected to the fiscal year 2018 fourth quarter population of 181,947 system-generated adjustments, we estimate that at least 96 percent of the system-generated accounting adjustments were recorded without

³²The preparation also includes verifying that a full accounting adjustment package is assembled, which includes the rationale for the adjustment, supporting documentation, approval at the appropriate thresholds, and verifying that the package satisfies the requirements outlined in the DOD FMR.

³³According to DFAS officials, all system-generated adjustments were initially categorized as unsupported. After sample testing is completed, if the testing demonstrates that a certain type of system-generated accounting adjustments is supported, DFAS will then categorize all adjustments related to the type of adjustments as supported.

adequate supporting documentation, which is required by DOD's policy and procedures and federal internal control standards.³⁴ In 2018, DFAS's auditor issued a finding identifying similar issues with DFAS's system-generated adjustments related to the scope of the eight narratives. As of November 2019, this finding was still open.

Standards for Internal Control in the Federal Government requires that management design control activities to achieve objectives and respond to risks, such as designing controls to help ensure accurate and timely recording and maintenance of appropriate transaction documentation.³⁵ Although the FMR has guidance on supporting documentation requirements for accounting adjustments, we found that DOD's FMR does not clearly define or include examples of what constitutes adequate supporting documentation of system-generated accounting adjustments. Specifically, the FMR does not differentiate between documentation requirements for manual and system-generated accounting adjustments. Rather, it states that reporting organizations must maintain adequate documentation, audit trails, and internal controls, and that the documentation must be made available upon request. Because system-generated accounting adjustments consist of summary-level financial information, DFAS officials stated that maintaining documentation at a detailed level would be impractical given the large volume of transactions at DOD.³⁶ However, without adequate supporting documentation for the business rules driving the recording of these adjustments, such as documentation of the programming logic for these adjustments, management and others cannot determine whether an adjustment was recorded for a valid reason or for the correct amount.

³⁴The estimate is 100 percent with a 95 percent confidence interval of (96.8, 100.0).

³⁵GAO, *Standards for Internal Control in the Federal Government*, [GAO-14-704G](#) (Washington, D.C.: September 2014), contains the internal control standards to be followed by executive agencies in establishing and maintaining systems of internal control as required by 31 U.S.C. § 3512 (c), (d) (commonly referred to as the Federal Managers' Financial Integrity Act).

³⁶DFAS records adjustments using both transaction-level and summary-level information for certain types of system-generated adjustments. For example, the balance in someone's checking account would be considered summary-level information. The balance is determined by transaction-level information, such as deposits and withdrawals. When DFAS records system-generated adjustments, it is unable to identify the individual transactions needing correction. It identifies a problem at the summary level, such as inconsistencies between different sources, and then forces one source to match the other without identifying the causes of inconsistencies.

DOD's Policies and Procedures for Categorizing Accounting Adjustments Do Not Reflect the Current Financial Reporting Environment

The March 2002 version of the DOD's FMR, volume 6A, chapter 2, established 10 category codes that are used to identify the circumstances under which accounting adjustments may be recorded.³⁷ For example, DFAS uses category A for reversing entries for a prior reporting period and category B for data call adjustments.³⁸ Additionally, the FMR specifies the required documentation needed to support each category. For example, for category A adjustments, adequate documentation includes information on the original entry and a statement that the adjustment is a reversing entry, whereas for category B adjustments, documentation requirements include information on the summarized amount and identification of the source or location of the transaction-level detail for the adjustment. DOD's core financial reporting system is designed to allow a DFAS accountant to select one of these 10 codes when recording an adjustment. Since these codes are used to identify the required documentation to support the adjustments, it is important that the codes are periodically reviewed to ensure that they are still relevant in DOD's current financial reporting environment and that supporting documentation requirements are appropriate.

We found that some of the category codes were rarely used and new codes may need to be added to reflect the current financial reporting environment. For example, we found that of the 18,521 manual adjustments recorded in DOD's core financial reporting system during the fourth quarter of fiscal year 2018, category F (supply management inventory) was used only four times. According to DFAS officials, this code was primarily used to adjust the purchase cost of certain supplies, but those adjustments are now rarely needed. DFAS officials stated that the codes had not been reviewed for continued relevance since they were first established and expressed a need to revisit the current categorization scheme to determine whether the codes should be redefined. The most

³⁷They are coded A through J, with each letter representing an adjustment for a given purpose.

³⁸Reversing entries, or reversing journal entries, are accounting adjustments recorded at the beginning of an accounting period to reverse or cancel out accounting adjustments recorded at the end of the previous accounting period. Data calls are accounting adjustments recorded for transactions where, because of timing or system issues, the financial information does not automatically transfer from source accounting systems and must be recorded with an adjustment instead. A typical data call transaction type is related to equipment. When equipment purchases and sales do not automatically transfer into the core financial reporting system, those transactions need to be recorded through adjustments.

recent update of FMR, volume 6A, chapter 2, in June 2019 included the addition of category M, the first code added since 2002.³⁹ According to DFAS officials, this code was not added based on a thorough review of the existing codes but because there was already a substantial volume of data call adjustments taking place in the Data Collection Module.

Further, a DOD official suggested that an additional code may be needed for tie-point adjustments, which DFAS accountants frequently record as a result of tie-point reconciliation.⁴⁰ We found that 34 of the 149 manual accounting adjustments we tested related to tie-point adjustments. Because there is not a designated category code for tie-point adjustments, we found that accountants used various other category codes when recording the 34 tie-point adjustments, including D (Recognition of Undistributed Disbursements and Collections), E (Reconciliation of Trial Balance and Budget Execution Reports), G (Reclassification of Accounts), H (Identified Errors and Reasonableness Checks), I (Adjustment to Balance Reports Internally), or at times no category code.⁴¹ As a result, there may be inconsistency in the documentation maintained to support tie-point adjustments. Having a single category code for tie-point adjustments could standardize recording by accountants, enabling DFAS to identify the frequency with which tie-point adjustments are recorded and ensure that it maintains adequate supporting documentation.

Standards for Internal Control in the Federal Government requires that management implement control activities through policies. To do this, management periodically reviews policies, procedures, and related control activities for continued relevance and effectiveness in achieving the organization's objectives or addressing related risks.⁴² The *DOD FMR*

³⁹Category M is for Data Collection Module. This adjustment records data call amounts from the Data Collection Module, which is a module of the DOD's core financial reporting system and a central repository for department-wide financial data used for consolidation and streamlining of data flow.

⁴⁰Tie-point reconciliations, also referred to as tie-points, are a series of standard financial management equations that indicate whether certain account balances within a general ledger balance are consistent with other account balances. When these account balances do not agree with one another, a tie-point adjustment may be necessary.

⁴¹A reclassification is an adjustment transferring an amount from one general ledger account to another. An example would be to reclassify an asset from property, plant, and equipment to inventory.

⁴²[GAO-14-704G](#).

Revision Standard Operating Procedures indicates that the FMR is reviewed every 2 years. However, based on our discussion with DOD officials, a thorough review of the category codes has not been performed and is needed to ensure the ongoing applicability of current category codes or the need for additional codes to reflect the current financial reporting environment. Without category codes for accounting adjustments that reflect current business needs, there is an increased risk that the reasons for recording these adjustments will not be properly captured and adequate supporting documentation will not be specified or maintained, hindering DFAS's ability to provide DOD management or auditors with reliable information about recorded accounting adjustments.

Policies and Procedures for Recording Accounting Adjustments Were Not Consistently Implemented

The FMR identifies critical elements that need to be included as part of the supporting documentation package when recording manual accounting adjustments. These elements include (1) correct appropriation and accounting information, (2) balanced adjustments, (3) approvals, (4) supporting documentation, and (5) valid *U.S. Standard General Ledger* (USSGL) account numbers.⁴³ The FMR further states that supporting documentation included in the package must include, among other things, elements to enable the assessment of the (1) accuracy and completeness of financial information recorded, (2) applicable criteria to support the reason for recording the adjustment, (3) specific expenditure or receipt accounts used, and (4) calculation of the dollar amount of the adjustment.

For the fourth quarter of fiscal year 2018, we selected a sample of manual and system-generated adjustments to determine if the supporting documentation for these adjustments included the critical elements described in DOD's FMR. We found that DFAS accountants did not consistently follow the DOD FMR and DFAS's policies and procedures for some of these critical elements, resulting in (1) the failure to maintain adequate supporting documentation, (2) the recording of out-of-balance

⁴³The Federal Financial Management Improvement Act of 1996, Pub. L. No. 104-208, div. A, § 101(f), title VIII, 110 Stat. 3009-389 (Sept. 30, 1996), requires major federal agencies to implement financial management systems that among other things comply with the USSGL at the transaction level. These standardized accounts help ensure the comparability of financial information across the federal government. The complete listing of six-digit USSGL accounts is established annually in the *Treasury Financial Manual*. The Department of the Treasury, *Chart of Accounts*, Bulletin No. 2018-08 (August 2018), pt. 1, sec. I.

accounting adjustments, and (3) the use of account numbers that do not comply with the USSGL.

- **Inadequate supporting documentation:** We found that 51 of the 87 manual adjustments we reviewed that DFAS categorized as supported did not contain supporting documentation required by the DOD FMR. For example, we found instances where supporting documentation packages were missing information to support the reason for recording the adjustment or detailed worksheets to support the calculation of the adjustment amount. DFAS officials explained that 30 of the 51 adjustments resulted from a major change in how DFAS processes U.S. Army Corps of Engineers' financial information. Because of time sensitivity and based on a risk analysis, management decided to process over 3,000 manual adjustments for the fourth quarter of fiscal year 2018, including the 30 that were selected for our sample, without preparing supporting documentation for these individual adjustments.

We also found that not all supporting documentation packages included a DFAS Form 9339, DFAS Journal Voucher Catalog and Checklist, as required by DFAS's Interim Policy Memorandum. This memorandum requires that all manual accounting adjustments, whether classified as supported or unsupported by DFAS, include a Form 9339 to help ensure the inclusion of the appropriate supporting documentation. We reviewed 149 manual adjustments and found that 94 included a Form 9339. Our review of these 94 accounting adjustments found that 28 lacked the required information. For example, nine packages did not include one or more of the necessary elements required by Form 9339.⁴⁴ We found instances where source information, customer coordination, document labeling, before and after trial balances, narratives, or a combination of these were missing. For six of the nine packages, DFAS agreed that some of the necessary data elements were missing; for the remaining three packages, DFAS's response did not fully address the reasons for the missing documentation. DFAS officials stated that one of the reasons why these errors may have occurred was because the implementation of the Interim Policy Memorandum was in its beginning stages when we selected our fourth quarter fiscal year 2018 sample. The policy

⁴⁴Section II of Form 9339 specifies information elements that are required to be included in a supporting package. These include elements such as the purpose, source information, descriptive document labeling, white paper/narratives, before and after accounting adjustment trial balances, and evidence of customer coordination.

memorandum was dated June 11, 2018, and was effective immediately.

We also found that 19 adjustments lacked the required root cause indicator code on the Form 9339.⁴⁵ According to DFAS officials, DFAS Cleveland prepared those 19 forms. DFAS Cleveland officials explained that in collaboration with the Navy Financial Management Office, DFAS Cleveland's senior leadership decided to deviate from the Interim Policy Memorandum and not include the root cause indicator code in the Form 9339 when recording Navy's related accounting adjustments. Rather, DFAS Cleveland developed its own system to identify root causes by using a unique identifier code. However, the Interim Policy Memorandum does not exclude any DFAS site from adhering to the requirement, and DFAS was unable to provide documentation to demonstrate that DFAS Cleveland had authorization to deviate from this policy. According to DFAS officials, DFAS Cleveland will begin including the root cause indicator code on the Form 9339, starting second quarter of fiscal year 2020.

- **Out-of-balance adjustments:** We found that about 2,800 manual adjustments, or approximately 15 percent of all manual adjustments recorded at the DOD consolidated level for the fourth quarter of fiscal year 2018, were out-of-balance. For example, we identified one adjustment in which DFAS decreased its FBWT account by \$14,232,000 without recording a change to a corresponding account. DOD's FMR requires that all recorded accounting adjustments be balanced. Additionally, we found that the FMR does not identify any situations where an out-of-balance adjustment is allowable, despite DFAS officials stating that out-of-balance adjustments are sometimes necessary.

Auditors of the military services found that reasons for out-of-balance financial information include (1) service-level general ledger systems are not effectively designed to prevent incomplete transactions from being recorded and (2) controls are not in place at the service level to detect these errors in a timely manner. According to DFAS officials, out-of-balance adjustments are recorded to correct out-of-balance

⁴⁵Section IV of Form 9339 requires accountants to identify and document a root cause indicator code for each adjustment. DFAS developed this code to identify the causes of accounting adjustments. The root cause indicator code is a four-part alphanumeric code that identifies (1) the system in which the adjustment was recorded, (2) the source of the information that needed adjusting, (3) a primary root cause indicator, and (4) a secondary root cause indicator.

financial information received from DOD components' accounting systems.

- **Use of non-USSGL-compliant accounts:** During our review of fourth quarter fiscal year 2018 manual and system-generated adjustments, we found that over 13,000 adjustments (over 6 percent) recorded at the DOD consolidated level used non-USSGL-compliant accounts, which are not allowed by the *Treasury Financial Manual* or DOD FMR. The Federal Financial Management Improvement Act of 1996 requires certain federal agencies, such as DOD, to use the specific and standardized set of accounts referred to as the USSGL in their financial reporting systems. Treasury maintains this set of accounts annually to help ensure the comparability of financial information across the federal government. DFAS officials stated that these noncompliant accounts are referred to as memo accounts and were primarily used for management planning purposes. They further explained that DOD had controls in place to prevent financial information recorded in memo accounts in DOD's core financial reporting system from being transferred into the financial reporting systems, which Treasury uses to compile the U.S. government consolidated financial statements.

DOD OIG also reported issues related to DOD's use of noncompliant accounts, which it identified in fiscal year 2018. In addition, in DOD's *Fiscal Year 2018 Agency Financial Report*, management acknowledged that DOD's financial management systems did not comply with the USSGL at the transaction level. In response, the DOD Deputy Chief Financial Officer issued a memorandum on March 15, 2019, acknowledging that DOD components must use the established USSGL accounts identified in the *Treasury Financial Manual* for financial reporting purposes. Additionally, the memorandum stated that supporting documentation must be maintained for any accounting adjustments recorded using memo accounts. However, for the seven non-USSGL-compliant adjustments included within our sample of manual and system-generated adjustments, we found that documentation had not been maintained.

Proper recording of adjustments is crucial for ensuring that the financial information accurately reflects the financial transactions that have occurred. This includes maintaining adequate supporting documentation and implementing review procedures to help ensure controls are in place to detect errors in a timely manner. Failure to fully adhere to established procedures increases the risk that inaccurate accounting adjustments will be recorded, thereby reducing the reliability of reported financial

information and potentially causing misstatements in the DOD consolidated financial statements.

DOD and DFAS Lack Policies and Procedures for Analyzing and Addressing Necessary Root Causes of Accounting Adjustments

Organizations use root cause analysis as a tool to identify and evaluate systems, processes, or both that prompted the recording of an accounting adjustment. For certain adjustments, it may be determined that a root cause analysis or action plan is not necessary—for instance, if the adjustment is onetime or nonroutine. However, information obtained through a root cause analysis may be used to make system or process changes within a specific program, thus reducing the need to record adjustments. Once a root cause has been identified and analyzed, an organization should create an action plan that describes the steps to be taken to address the root cause and monitors the effectiveness of the actions taken. Figure 5 illustrates the identification, implementation, and monitoring of accounting adjustment root causes and related action plans.

Figure 5: Identification and Analysis of Root Cause and the Implementation and Monitoring of Action Plans for Accounting Adjustments



Source: GAO analysis of Office of Management and Budget Circular A-123. | GAO 20-96

We found that although DFAS headquarters and its individual sites perform root cause analysis and develop and take some actions to address the identified causes, neither DOD nor DFAS has established policies and procedures that require staff to perform root cause analysis; develop and implement action plans for issues that DFAS staff identified; or monitor the effectiveness of action plans in eliminating the need for accounting adjustments. DFAS officials acknowledged that there are no policies in place requiring DFAS to perform root cause analyses that would permit them to compare root causes for accounting adjustments at a consolidated level across the DFAS sites.

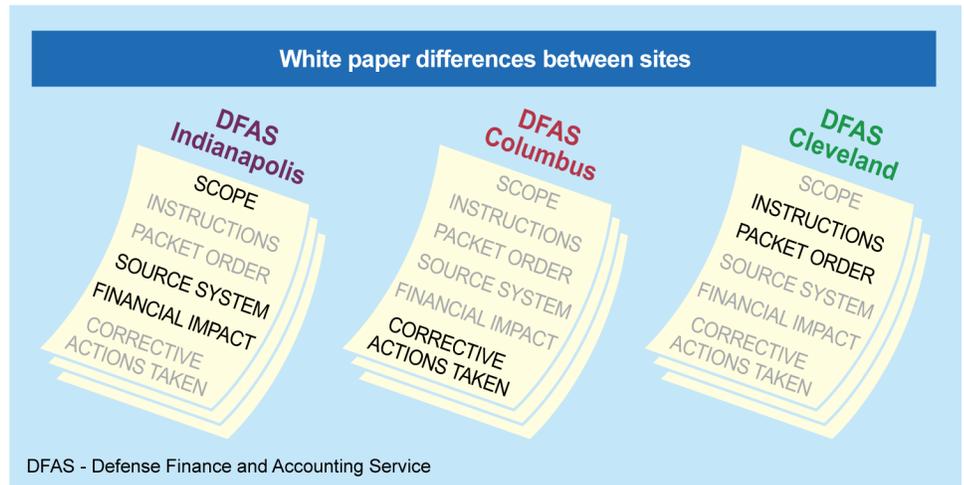
DFAS and its sites identify root causes for individual accounting adjustments when accountants select a root cause indicator code when recording the adjustment. DFAS staff also identify root causes for accounting adjustments at an aggregate level when preparing summary metrics on adjustment types. For example, we found that in addition to the requirements previously discussed, Form 9339 requires accountants across all DFAS sites to prepare “white papers/narratives (white papers) each time a manual adjustment is recorded.”⁴⁶ Our review of these white papers identified that some DFAS sites use the white papers to document the root cause analyses while others do not because DFAS has not provided a template that identifies the minimum required information to be included in the white papers. As a result, we found that individual DFAS sites do not use standardized white paper templates and that the information included in the white papers was not always consistent between and within the DFAS sites.

- **Inconsistency between DFAS sites:** Our review of 52 white papers found that DFAS Indianapolis was the only site to include information such as scope, source system, and financial statement impact of the accounting adjustment in its white papers, while DFAS Columbus was the only site that included corrective actions taken.⁴⁷ (See fig. 6.)

⁴⁶The description in DFAS Form 9339 is as follows: “The White Paper/Narrative explains the role each page included in the JV package plays in the adjustment, i.e. reason, regulatory guidance, specific *Treasury Financial Manual* transaction used in the adjustment, system limitations, applicable System Change Requests, and description and purpose of supporting documentation.”

⁴⁷We reviewed 52 white papers/narratives across three DFAS sites. Specifically, we reviewed 21 white papers prepared by DFAS Indianapolis, 10 prepared by DFAS Columbus, and 21 prepared by DFAS Cleveland.

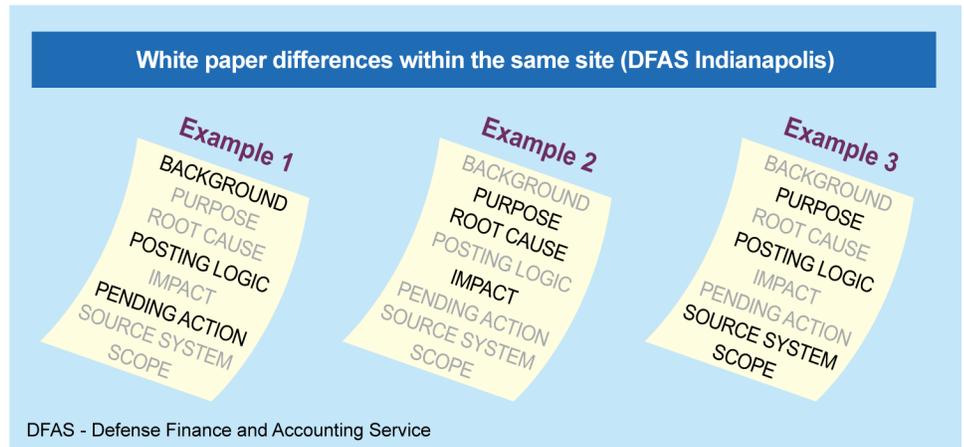
Figure 6: Inconsistency of Information in White Papers between DFAS Sites



Source: GAO analysis of Department of Defense information. | GAO 20-96

- **Inconsistency within a DFAS site:** Our review of 52 white papers found that DFAS Indianapolis did not consistently include background, purpose of the adjustment, a description of the root cause, posting logic, financial statement impact, pending action, source system, and scope in all white papers it prepared. Some white papers had these elements and others did not. We found similar issues with the white papers prepared by DFAS Columbus and DFAS Cleveland. Figure 7 illustrates information included in white papers that was inconsistent within a DFAS site.

Figure 7: Inconsistency of Information in White Papers within a DFAS Site



Source: GAO analysis of Department of Defense information. | GAO 20-96

We also found that DFAS does not have policies and procedures requiring the identification and implementation of action plans to address the cause of and need for accounting adjustments that staff identified internally. This resulted in inconsistencies in how the different DFAS sites developed and implemented action plans. For example, we found that 73 of the 98 manual and system-generated unsupported adjustment packages that included a root cause analysis that we reviewed did not include an action plan to address the root cause. Based on this testing, we estimate that at least 88 percent of fourth quarter fiscal year 2018 unsupported adjustments for which a root cause analysis was performed did not have a documented action plan.⁴⁸ For the remaining 25 packages with documented action plans, we found that only two included steps documenting how the action plan was to be implemented. The remaining 23 packages with documented action plans lacked implementation details, and DFAS officials stated that they were waiting for resolution from the relevant DOD components.

DFAS officials stated that they prepare and document action plans for issues that affect multiple accounting adjustments but not for issues that affect only one adjustment (unique root cause). Unique root causes do not necessitate action plans and are resolved the following month through

⁴⁸The estimate is 97.6 percent with a 95 percent confidence interval of (88.5, 99.9).

DFAS working with the affected DOD components. According to DFAS officials, many of the action plans are discussed in biweekly and monthly meetings, but these action plans are not documented.

Finally, we found that DOD and DFAS do not have policies and procedures requiring management to monitor the results of action plans that individual DFAS sites prepared or to measure whether implemented action plans are effective in addressing the causes for accounting adjustments. DFAS management activities were limited to periodically reviewing summary metrics on the numbers and types of accounting adjustments recorded. These metrics did not contain detailed information, such as the causes of accounting adjustments to be addressed, accountable officials responsible for implementing action plans, expected time frames for the implementation of action plans, or specific steps to be performed to address the causes. Additionally, the metrics did not include any information on action plans to address system-generated accounting adjustments, which account for the majority of the adjustments. This type of detailed information is critical to DOD management and DOD external stakeholders for evaluating the department's progress in correcting the issues. GAO has previously reported that a lack of comprehensive information on corrective action plans limits DOD's and Congress's ability to evaluate DOD's progress toward fully, timely, and efficiently correcting its long-standing financial management deficiencies.

Office of Management and Budget Circular A-123 requires agencies to perform cause analysis of deficiencies identified to ensure that subsequent strategies and plans address the causes of the problem and not just the symptoms.⁴⁹ Additionally, *Standards for Internal Control in the Federal Government* requires that management implement control activities through policies. To do this, management documents in its policies the internal control responsibilities of the organization. In addition, management periodically reviews policies, procedures, and related control activities for continued relevance and effectiveness in achieving the entity's objectives or addressing related risks.⁵⁰ Without policies that require consistent processes across DOD for identifying and addressing the causes of accounting adjustments, from the identification of underlying root causes to the development, implementation, and

⁴⁹Office of Management and Budget, *Management's Responsibility for Enterprise Risk Management and Internal Control*, Circular No. A-123 (July 15, 2016).

⁵⁰[GAO-14-704G](#).

monitoring of action plans, it is likely that DOD's efforts to reduce accounting adjustments will be inefficient and ineffective.

DOD and DFAS Have Taken Actions to Reduce Accounting Adjustments but Lack Procedures for Implementing a Department-Wide Strategy

The large number of accounting adjustments that are recorded in the preparation of DOD's financial statements presents audit challenges. To address this issue, DOD and DFAS have established multiple initiatives aimed at reducing accounting adjustments. While these initiatives have resulted in fewer adjustments of certain types being recorded at the component and consolidated levels, the current focus has been on reducing the number of adjustments recorded without adequate supporting documentation within their responsible work areas, not on reducing the need for recording accounting adjustments department-wide.

Both DFAS and OUSD (Comptroller) have developed department-wide strategies to decrease accounting adjustments; however, neither DFAS nor OUSD (Comptroller) have developed procedures for implementing the department-wide strategies. Without a clear department-wide approach to reducing accounting adjustments across all DOD components, there is a risk that DOD's effort to reduce accounting adjustments will be unsuccessful, which in turn hinders its ability to produce reliable and auditable consolidated financial statements.

DOD Has Undertaken Initiatives to Reduce Accounting Adjustments

To reduce accounting adjustments, OUSD (Comptroller) and DFAS have undertaken many initiatives over the last few years. In fiscal year 2018, OUSD (Comptroller) determined that a large number of accounting adjustments at the consolidated level resulted from data calls. To decrease the need for recording these adjustments at the consolidated level, DOD established the Data Call Journal Voucher (JV) Migration Initiative with the goal of eliminating data call adjustments in its core financial reporting system to the maximum extent possible.

The first phase of this initiative moved the recording of adjustments for the Federal Employees' Compensation Act (FECA) liability to the DOD component level responsible for the underlying transaction. According to OUSD (Comptroller), this initiative resulted in the successful migration of the recording of the Missile Defense Agency's FECA liability from DOD's core financial reporting system to Missile Defense Agency accounting systems in the second quarter of fiscal year 2019, and has set the stage for 19 other components using the same accounting system as the

agency to follow suit.⁵¹ Although this initiative may not reduce the overall number of accounting adjustments that DOD records, it will reduce the need for data call adjustments to be recorded at the consolidated level. OUSD (Comptroller) expects this initiative will also enhance the quality of the supporting documentation maintained for these types of adjustments because the underlying transaction-level detail for the adjustments will be available in the components' accounting systems.

Individual DFAS sites have also undertaken their own initiatives that eliminate the need for some accounting adjustments. For example, in fiscal year 2018, DFAS Indianapolis found that some financial information from the Army's accounting systems was improperly recorded, requiring adjustments to correct the errors when the financial information transferred into the DOD's core financial reporting system. DFAS Indianapolis staff worked with the Army to resolve the issue. As a result, adjustments are no longer needed at the consolidated level when the information transfers from Army's system into DFAS's system. According to DFAS Indianapolis officials, this initiative resulted in a significant decrease in accounting adjustments at the consolidated level for fiscal year 2019.⁵²

DOD and DFAS Lack Procedures for Implementing a Department-Wide Strategy to Reduce the Need for Accounting Adjustments

Developing and implementing a DOD department-wide strategy to reduce the need for recording accounting adjustments at the consolidated level requires DOD to identify the underlying root causes and risks associated with accounting adjustments and to prioritize efforts to address them. This involves clearly defining what is to be done, who is to do it, how it will be done, and the time frames for achievement. To address DOD's many financial management issues, including reducing accounting adjustments, OUSD (Comptroller) and DFAS have developed different strategies and business plans. However, these strategies and business plans do not include clearly defined expected outcomes or procedures for achieving stated goals.

OUSD (Comptroller) issued the *DOD Financial Management Strategy Fiscal Years 2016–2020* (Strategy) to help achieve a simplified, standard,

⁵¹FECA is the federal law that requires compensation be paid for the disability or death of a federal employee resulting from personal injury sustained while performing his or her duties. 5 U.S.C. §§ 8101-8193.

⁵²According to DFAS Indianapolis officials, this initiative resulted in an approximately \$18.1 billion decrease in accounting adjustments.

affordable, auditable, and secure financial environment, which includes the reduction of accounting adjustments. The Strategy's JV initiative states that "The purpose of this initiative is to determine why unsupported JVs occur and resolve them." However, we found that the Strategy did not provide clear direction to staff on how to achieve the JV initiative and did not call for a department-wide effort to address accounting adjustments recorded at the consolidated level. The Strategy also acknowledged that excessive adjustments can indicate underlying problems, such as weak internal controls, and may indicate that transactions are not captured, reported, or summarized correctly. However, we found that the focus of the Strategy was on reducing the number of accounting adjustments recorded without adequate supporting documentation rather than on reducing the overall need for recording accounting adjustments department-wide.

In addition to following the OUSD's (Comptroller) Strategy, DFAS management has also developed the *Fiscal Years 2017—2021 Strategic Plan* (Strategic Plan) and *Fiscal Year 2018 Annual Business Plan* (Business Plan), which include goals for reducing accounting adjustments, supplemented by bimonthly Strategy Updates.⁵³ For example, DFAS's November 2017 Strategy Update outlined the Business Plan goals for fiscal year 2018 with regard to internal controls and business processes. In that update, DFAS set broad goals, such as executing plans to support or reduce system-generated and manual adjustments. However, we found that similar to the OUSD (Comptroller) Strategy, neither DFAS's Strategic Plan nor Business Plan included defined outcomes or clear procedures for accomplishing the stated goals.

The primary focus of these goals was also to reduce the number of accounting adjustments recorded without adequate supporting documentation. We found that this lack of clear procedures led each DFAS site and DFAS headquarters to focus their initiatives on accounting adjustments that impacted their responsible work areas instead of reducing the need for recording accounting adjustments overall. According to DFAS site officials, in some instances, reducing the number of accounting adjustments recorded without adequate supporting documentation at their individual sites could have an impact on the need

⁵³At Strategy Update meetings, DFAS headquarters and sites update DFAS senior leadership on progress toward their individual goals.

to record adjustments at the consolidated level; however, the effect at the consolidated level was not their primary focus.

Standards for Internal Control in the Federal Government requires that management implement control activities through policies. To do this, management documents in its policies the internal control responsibilities of the organization. In addition, management periodically reviews policies, procedures, and related control activities for continued relevance and effectiveness in achieving the entity's objectives or addressing related risks.⁵⁴ Without detailed documented policies and procedures for implementing its initiatives, and a complete understanding of the issues contributing to the recording of accounting adjustments (both supported and unsupported) across DOD, there is an increased risk that management efforts to reduce accounting adjustments at the consolidated level will be ineffective.

Conclusions

In the routine course of business, organizations often record accounting adjustments on a monthly, quarterly, and annual basis. Some adjustments are necessary so that financial information is presented meaningfully and accurately. However, an extensive use of accounting adjustments may indicate significant underlying problems.

In order to produce reliable financial information that DOD management and Congress can use for decision-making, DOD needs to develop policies and procedures for recording accounting adjustments that are consistently implemented across the department and reflect the current DOD financial reporting environment. DOD also needs to address the issues that contribute to its need to extensively record accounting adjustments by implementing policies and procedures for the consistent identification of the causes for recording adjustments and the development, implementation, and monitoring of action plans to address the identified causes. If DOD does not address these issues, there is an increased risk that its financial information will be misstated and DOD will continue to be unable to prepare reliable and auditable consolidated financial statements.

⁵⁴[GAO-14-704G](#).

Recommendations for Executive Action

We are making the following eight recommendations to DOD:

- The Director of DFAS should, in accordance with the FMR, implement procedures to help ensure that FBWT reconciliations are consistently performed and that all DFAS sites review and document research conducted on the causes of any differences arising from these reconciliations. (Recommendation 1)
- The Under Secretary of Defense (Comptroller) should update the FMR to clearly define the required supporting documentation for system-generated accounting adjustments, including the required documentation of business rules driving the recording of these adjustments, such as documentation of the programming logic. (Recommendation 2)
- The Under Secretary of Defense (Comptroller) should perform and document a comprehensive review of the FMR accounting adjustment category codes to determine their ongoing applicability or the need for additional codes to reflect the current financial reporting environment. (Recommendation 3)
- The Under Secretary of Defense (Comptroller) should establish procedures to help ensure the consistent implementation of the requirements of DFAS Form 9339. (Recommendation 4)
- The Under Secretary of Defense (Comptroller) should update policies and procedures to identify the causes of out-of-balance accounting adjustments and resolve the causes in a timely manner. (Recommendation 5)
- The Under Secretary of Defense (Comptroller), in conjunction with the Director of DFAS, should develop and implement policies and procedures to help ensure that root cause analyses for accounting adjustments are consistently performed and documented across DOD. (Recommendation 6)
- The Under Secretary of Defense (Comptroller), in conjunction with the Director of DFAS, should develop and implement policies and procedures to help ensure consistent development, implementation, monitoring, and documentation of action plans across DOD that address accounting adjustment causes that staff identified internally. (Recommendation 7)
- The Under Secretary of Defense (Comptroller), in conjunction with the Director of DFAS, should develop and implement procedures across DOD that include clearly defined outcomes focused on reducing accounting adjustments (supported and unsupported) with specific

actionable steps and procedures for achieving stated goals.
(Recommendation 8)

Agency Comments and Our Evaluation

We provided a draft of this report to DOD for review and comment. In written comments, DOD concurred with all eight of our recommendations and cited actions to address them. DOD's comments are reproduced in appendix II.

As agreed with your office, unless you publicly announce the contents of this report earlier, we plan no further distribution until 11 days from the report date. At that time, we will send copies of this report to the appropriate congressional committees, the Secretary of Defense, the Under Secretary of Defense (Comptroller), the Director of the Defense Finance and Accounting Service and other interested parties. In addition, the report is available at no charge on the GAO website at <http://www.gao.gov>.

If you or your staff have any questions about this report, please contact me at (202) 512-2989 or kociolek@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix III.



Kristen Kociolek
Director
Financial Management and Assurance

Appendix I: Objectives, Scope, and Methodology

This report examines (1) accounting adjustments and their effect on the reliability of the Department of Defense's (DOD) financial information, (2) the extent to which DOD has established and implemented policies and procedures for recording accounting adjustments, and (3) the extent to which DOD has taken actions to reduce accounting adjustments recorded at the consolidated level.

To determine the accounting adjustments recorded and their effect on the reliability of DOD's financial information, we focused our review on the categories of accounting adjustments that DOD recorded at the consolidated level.¹ We reviewed prior audit reports issued by GAO, DOD's Office of Inspector General (OIG), and independent public accountants for fiscal years 2015 through 2019 to gain an understanding of the types and categories of accounting adjustments. We also reviewed related policies and procedures, such as DOD's *Financial Management Regulation* (FMR); performed walk-throughs of the Defense Finance and Accounting Service's (DFAS) processing of accounting adjustments; and interviewed DOD officials to gain an understanding of the types of accounting adjustments. Additionally, we obtained and analyzed summary information on the adjustments affecting fiscal years 2017 and 2018 by quantity, dollar value, whether they were manual versus system-generated, and unsupported versus supported.

To evaluate the extent to which DOD has established and implemented policies and procedures for recording accounting adjustments, we reviewed relevant notices of finding and recommendation that the independent public accountants and DOD OIG issued related to accounting adjustments for fiscal year 2018. We also reviewed DOD and DFAS policies and procedures and interviewed officials from DFAS and the Office of the Under Secretary of Defense (OUSD) (Comptroller) to identify issues surrounding accounting adjustments and the procedures used to process, review, and approve these adjustments in DOD systems. We also inquired about the procedures used to determine the underlying causes of accounting adjustments, if action plans to address the causes had been developed, and the status of these plans. In

¹For the purposes of this report, consolidated level is defined as all adjustments processed in three modules within DOD's Defense Departmental Reporting System (DDRS). Specifically, we reviewed the DDRS—Budgetary (DDRS-B), DDRS—Audited Financial Statements (DDRS-AFS) and DDRS-AFS Beginning Balance Adjustment modules.

addition, we assessed DFAS's efforts to monitor the effectiveness of its action plans.

To determine the specific internal controls DOD had in place over its accounting adjustment processes, we interviewed DFAS officials knowledgeable about the accounting adjustment processes and performed walk-throughs of these processes at DFAS. We evaluated the procedures observed during our walk-throughs and those that DOD officials described to determine whether DFAS recorded adjustments in accordance with established policies and procedures. For issues identified, we interviewed DOD officials to confirm our understanding and determined the reasons for the issues identified.

To determine if DOD had designed and implemented internal controls over its accounting adjustment processes, we analyzed the information we obtained through the interviews and walk-throughs using relevant criteria, including the DOD FMR, the *Treasury Financial Manual*, and our *Standards for Internal Control in the Federal Government*.² We also performed tests of controls on a random sample of 242 accounting adjustments from a population of 200,468 adjustments that DFAS recorded at the consolidated level that impacted the financial statements for the fourth quarter of fiscal year 2018. The selected adjustments were recorded in the Defense Departmental Reporting System (DDRS)—Budgetary (DDRS-B), DDRS—Audited Financial Statements (DDRS-AFS), and DDRS-AFS Beginning Balance Adjustment modules. From the DDRS-B and DDRS-AFS modules, we selected a random sample of 225 accounting adjustments, and from the DDRS-AFS Beginning Balance Adjustment module we selected all 17 accounting adjustments. From the three different sets of data, we stratified the selected accounting adjustments into six strata (see table 1).

²GAO, *Standards for Internal Control in the Federal Government*, [GAO-14-704G](#) (Washington, D.C.: September 2014).

Table 1: Selected Accounting Adjustments Sample

No.	Strata	Total adjustments tested	Manual adjustments tested	System-generated adjustments tested
1	All adjustments within the Defense Departmental Reporting System—Audited Financial Statements Beginning Balance Adjustments	17	17	0
2	Adjustments labeled “Supported” within Defense Departmental Reporting System—Audited Financial Statements	45	45	0
3	Adjustments labeled “Unsupported” within Defense Departmental Reporting System—Audited Financial Statements	45	45	0
4	Adjustments labeled “Supported” within Defense Departmental Reporting System—Budgetary	45	8	37
5	Adjustments labeled “Unsupported” within Defense Departmental Reporting System—Budgetary	45	3	42
6	Out-of-balance adjustments within Defense Departmental Reporting System—Budgetary	45	31	14
Total		242	149	93

Source: GAO based on selection of sample for testing. | GAO-20-96

Note: We performed tests of controls on a random sample of 242 accounting adjustments from a population of 200,468 adjustments recorded at the consolidated level that impacted the fourth quarter of fiscal year 2018. We were able to project the results of testing of the randomly selected sample to the population of accounting adjustments. We designed the sample to support estimation for all accounting adjustments with a margin of error no greater than plus or minus 8.4 percentage points at the 95 percent level of confidence.

Of the total 242 adjustments, we selected all 17 adjustments in stratum 1, and 45 adjustments each from strata 2 through 6 for testing. We designed the sample to support estimation for all supported accounting adjustments with a margin of error no greater than plus or minus 11.7 percentage points at the 95 percent level of confidence, estimation for all unsupported accounting adjustments with a margin of error no greater than plus or minus 11.8 percentage points at the 95 percent level of confidence, and estimation overall for all accounting adjustments with a margin of error no greater than plus or minus 8.4 percentage points at the 95 percent level of confidence.

Because we followed a probability procedure based on random selections, our sample is only one of a large number of samples that we might have drawn. Since each sample could have provided different estimates, we express our confidence in the precision of our particular sample’s results as a 95 percent confidence interval (e.g., plus or minus 8 percentage points). This is the interval that would contain the actual population value for 95 percent of the samples we could have drawn.

For the accounting adjustments in our sample that DOD considered supported, we reviewed underlying documentation to determine whether the adjustments were properly supported and contained all critical elements required by DOD policy. We then shared the results of testing with DOD and incorporated any applicable additional information DOD officials provided into our analysis, as appropriate. As part of our testing, we also reviewed documentation related to unsupported accounting adjustments selected in our sample and interviewed DFAS officials to determine if DOD had performed root cause analyses, developed action plans to address the identified causes, and taken any actions in response. We then shared the results of testing with DOD and incorporated any applicable additional information DOD officials provided into our analysis, as appropriate.

To assess the reliability of the accounting adjustment information we received from DOD, we conducted interviews with relevant agency officials, compared summary-level dollar amounts and quantities to another DOD information source, performed electronic testing of the financial information, and reviewed related internal controls. On the basis of this work, we found the financial information to be sufficiently reliable to project results of our random sample testing to the population of accounting adjustments for the fourth quarter of fiscal year 2018. Margins of error varied depending on the specific stratum being projected and are disclosed with all estimates contained within the report.

To determine the extent to which DOD has taken actions to reduce accounting adjustments recorded at the consolidated level that may affect the reliability of its financial information, we interviewed officials from DFAS and the OUSD (Comptroller) to identify initiatives aimed at reducing accounting adjustments. We further inquired about what tools DFAS used to measure its progress and analyzed summary metrics provided from fiscal years 2017 to 2018 to determine the effect of these efforts on the number of accounting adjustments recorded during these periods.

We conducted this performance audit from November 2018 to January 2020 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Comments from the Department of Defense



COMPTROLLER

OFFICE OF THE UNDER SECRETARY OF DEFENSE
1100 DEFENSE PENTAGON
WASHINGTON, DC 20301-1100

DEC 05 2019

Ms. Kristen Kociolek
Director, Financial Management and Assurance
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Ms. Kociolek:

This is the Department of Defense (DoD) response to the Government Accountability Office (GAO) Draft Report GAO-20-096 "DEPARTMENT OF DEFENSE: Actions Needed to Reduce Accounting Adjustments," dated November 13, 2019 (GAO Code 103169). Enclosed are our responses to the recommendations directed to the Secretary of Defense and the Under Secretary of Defense (Comptroller)/Chief Financial Officer.

My office has reviewed the draft report and associated recommendations. As a result, the Department is actively developing strategies to reduce accounting adjustments. Subsequently, the Department will update the Department of Defense Financial Management Regulation and document strategies with specific outcomes and detailed procedures for achieving stated goals in the strategies.

We appreciate the opportunity to review and comment on the GAO draft report. My point of contact is Ms. Krystal Baranoski, at krystal.j.baranoski.civ@mail.mil and 703-695-7193.

Sincerely,

Mark E. Easton
Deputy Chief Financial Officer

Enclosure:
As stated



GAO Draft Report Date November 13, 2019
GAO-20-96 (GAO CODE 103169)

“DEPARTMENT OF DEFENSE: Actions needed to Reduce Accounting Adjustments”

**OFFICE OF THE UNDER SECRETARY OF DEFENSE (COMPTROLLER) (OUSDC)
RESPONSES TO THE GAO RECOMMENDATIONS, INCLUDING ONE ON BEHALF
OF THE DEFENSE FINANCE AND ACCOUNTING SERVICE**

RECOMMENDATION 1: “The Director of DFAS, should in accordance with the FMR, implement procedures to help ensure that Fund Balance with Treasury reconciliations are consistently performed and research conducted on the causes of any difference arising from these reconciliations is reviewed and documented by all DFAS sites.”

DEFENSE FINANCE AND ACCOUNTING SERVICE (DFAS) RESPONSE: Concur. The Defense Finance and Accounting Service (DFAS) will implement procedures to help ensure Fund Balance with Treasury (FBwT) reconciliations are performed consistently and appropriate research on the causes of any difference arising from these reconciliations is reviewed and documented by all DFAS sites.

RECOMMENDATION 2: “The Office of the Under Secretary of Defense (Comptroller) should update the Financial Management Regulation to clearly define the required supporting documentation for system-generated accounting adjustments including the required documentation of business rules driving the recording of these adjustments such as documentation of the programming logic.”

OUSDC RESPONSE: Concur. The Department is developing a checklist of required supporting documents for incorporation into the DoD Financial Management Regulation (FMR).

RECOMMENDATION 3: “The Office of the Under Secretary of Defense (Comptroller) should perform and document a comprehensive review of the FMR accounting adjustment category codes to determine their ongoing applicability or the need for additional codes to reflect the current financial reporting environment.”

OUSDC RESPONSE: Concur. The Department intends to collaborate with the financial community to update the category codes within the DoD FMR.

RECOMMENDATION 4: “The Office of the Under Secretary of Defense (Comptroller) should establish procedures to help ensure the consistent implementation of the requirements of Form 9339.”

OUSD(C) RESPONSE: Concur. The Department is introducing a plan to require a refresher course to all users of the Form 9339.

RECOMMENDATION 5: “The Office of the Under Secretary of Defense (Comptroller) should update policies and procedures to identify the causes of out-of-balance accounting adjustments and resolve the causes in a timely manner.”

OUSD(C) RESPONSE: Concur. The Department is collaborating on utilizing existing data to identify and resolve out-of-balances and update the policies and procedures.

RECOMMENDATION 6: “The Office of the Under Secretary of Defense (Comptroller) in conjunction with the Director of DFAS should develop and implement policies and procedures to help ensure that root causes analyses for accounting adjustments are consistently performed and documented across DOD.”

OUSD(C) RESPONSE: Concur. The Department, in conjunction with the Director of DFAS, intends to utilize existing advanced analytics tools to research and document root cause analyses.

RECOMMENDATION 7: “The Office of the Under Secretary of Defense (Comptroller) in conjunction with the Director of DFAS should develop and implement policies and procedures to help ensure consistent development, implementation, monitoring, and documentation of action plans across DOD that address accounting adjustment causes identified internally by staff.”

OUSD(C) RESPONSE: Concur. The Department intends to collaborate with the financial community, including the Director of DFAS, and utilize existing tools for documenting and implementing consistent procedures for action plans of accounting adjustments.

RECOMMENDATION 8: “The Office of the Under Secretary of Defense (Comptroller) in conjunction with the Director of DFAS should develop and implement procedures across DOD that include clearly defined outcomes focused on reducing accounting adjustments (supported and unsupported) with specific actionable steps and procedures for achieving stated goals.”

OUSD(C) RESPONSE: Concur. The Department, in conjunction with the Director of DFAS, plans to utilize existing tools to define and measure the outcomes of accounting adjustments.

Appendix III: GAO Contact and Staff Acknowledgments

GAO Contact

Kristen Kociolek, (202)512-2989 or kociolekk@gao.gov

Staff Acknowledgments

In addition to the contact named above, Kimberley McGatlin (Assistant Director), Carl Barden, Rathi Bose, Veronica Cadiz-Rodriguez, Virginia Chanley, Benjamin Durfee, Patrick Frey, Maxine Hattery, Jason Kelly, Jason Kirwan, Zhen Li, John Lopez, Samuel Sawhook, Dacia Stewart, and Anne Thomas made key contributions to this report.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through our website. Each weekday afternoon, GAO posts on its [website](#) newly released reports, testimony, and correspondence. You can also [subscribe](#) to GAO's email updates to receive notification of newly posted products.

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's website, <https://www.gao.gov/ordering.htm>.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

Connect with GAO

Connect with GAO on [Facebook](#), [Flickr](#), [Twitter](#), and [YouTube](#).
Subscribe to our [RSS Feeds](#) or [Email Updates](#). Listen to our [Podcasts](#).
Visit GAO on the web at <https://www.gao.gov>.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact FraudNet:

Website: <https://www.gao.gov/fraudnet/fraudnet.htm>

Automated answering system: (800) 424-5454 or (202) 512-7700

Congressional Relations

Orice Williams Brown, Managing Director, WilliamsO@gao.gov, (202) 512-4400,
U.S. Government Accountability Office, 441 G Street NW, Room 7125,
Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548

Strategic Planning and External Liaison

James-Christian Blockwood, Managing Director, spel@gao.gov, (202) 512-4707
U.S. Government Accountability Office, 441 G Street NW, Room 7814,
Washington, DC 20548

