

May 2009

**FINANCIAL
MANAGEMENT**

**Achieving Financial
Statement Auditability
in the Department of
Defense**



GAO

Accountability * Integrity * Reliability

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United States Government Accountability Office
Washington, DC 20548

May 6, 2009

Congressional Requesters

Since the first financial statement audit was attempted at a major Department of Defense (DOD) component over 20 years ago, GAO and DOD auditors have continued to report significant weaknesses in the department's ability to provide timely, reliable, consistent, and accurate information for management analysis, decision-making, and reporting. DOD has undertaken a number of initiatives over the years, such as the Financial Improvement Initiative in 2003, to improve the department's business operations, including financial management, and achieve clean financial statement audit opinions. However, these initiatives have met with limited success. In 2005, the DOD Comptroller established the DOD Financial Improvement and Audit Readiness (FIAR) Directorate¹ to manage DOD-wide financial improvement efforts and to integrate those efforts with transformation activities, such as those outlined in the Enterprise Transition Plan,² across the department. The components report accomplishments and progress against planned corrective actions to the FIAR Directorate for reporting in the FIAR Plan.

You asked us to analyze the department's FIAR Plan to identify any areas where improvements are needed to enhance the plan's effectiveness as a management tool for guiding, monitoring, and reporting on the department's efforts to identify and resolve its financial management weaknesses and achieve financial statement auditability. On March 11, 2009 and on March 27, 2009, we briefed your offices on the results of this work. This letter summarizes the information provided during the briefing and the attached briefing slides have been updated with additional information as of April 24, 2009. The full briefing, including our scope and methodology, can be found in appendix I.

We performed our review from October 2008 through May 2009 in accordance with generally accepted government auditing standards. Those

¹The FIAR Directorate is responsible for preparing the FIAR Plan to comply with provisions in the National Defense Authorization Act for Fiscal Year 2002 and subsequent provisions in the Authorization Acts for fiscal years 2006 and 2007.

²DOD considers the Enterprise Transition Plan its department-wide plan for business transformation.

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 the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Results in Brief

In 2004, we reported that DOD lacked a comprehensive and integrated strategic plan with key milestones, measures/metrics, accountability mechanisms, or cost estimates for achieving financial statement auditability.³ According to best practices, a strategic plan should include the following key elements:

- provide a comprehensive view of performance, including the establishment of a baseline of current operational functions, capabilities, and performance against which progress toward a defined goal or objective can be measured;
- align goals and measures with departmentwide goals, and cascading goals and measures to lower organizational levels;
- establish timelines and demonstrate results;
- assign accountability for achieving results; and
- link resource needs to performance.⁴

While the FIAR Plan identifies three goals for improving DOD financial information and achieving audit readiness, it does not contain the key elements of a strategic plan that we have previously reported as necessary for successful DOD business transformation. During our review of DOD's September 2008 FIAR Plan, we identified the following areas that the department needs to address to improve the FIAR Plan as a strategic and management tool:

- clear guidance is needed in developing and implementing improvement efforts;
- no clear baseline exists against which incremental progress can be measured;

³GAO, *Financial Management: Further Actions Are Needed to Establish Framework to Guide Audit Opinion and Business Management Improvement Efforts at DOD*, [GAO-04-910R](#) (Washington, D.C.: Sept. 20, 2004).

⁴See GAO, *Defense Business Transformation: Achieving Success Requires a Chief Management Officer to Provide Focus and Sustained Leadership*, [GAO-07-1072](#) (Washington, D.C.: Sept. 5, 2007); and as stipulated by the Government Performance and Results Act of 1993.

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- linkages between FIAR Plan goals and corrective actions and reported accomplishments are not always clear;
 - clear results-oriented metrics for measuring and reporting incremental progress are needed, and
 - accountability is not clearly defined or assigned and resources budgeted and consumed are not identified.

We also identified recent actions the department is taking to begin to address many of the issues we have identified above.

Clear Guidance Is Needed in Developing and Implementing Improvement Efforts

Although DOD's September 2008 FIAR Plan emphasizes the importance of activities to identify and correct the department's financial management weaknesses and achieve financial statement auditability, further clarity is needed. We found that the FIAR Plan does not provide clear guidance to DOD components for developing consistent and compatible FIPs. For example, while the FIAR Plan provides examples of the types of activities that should occur within DOD components to identify financial management weaknesses, it is unclear which specific office or organization within an entity is accountable for performing these activities or tasks. This delineation of accountability is of particular importance in situations in which a policy, process and control, or system is controlled at the department level and is not within a component's control to change. Additionally, it is unclear what process or methodology a component should apply to identify and coordinate FIP efforts with those of other ongoing transformation efforts within the department or a component such as efforts to achieve total asset visibility.⁵ The lack of clear guidance in developing and implementing improvement efforts can result in premature or unjustified management assertions regarding the audit readiness of reported financial information based on inadequate and insufficient corrective actions taken in support of assertions.

No Clear Baseline Exists against Which Incremental Progress Can Be Measured

The FIAR Plan does not establish a baseline of the department's financial management weaknesses and capabilities—such a baseline could be used to measure incremental progress toward achieving an estimated milestone date established for each component and the department. For example,

⁵DOD defines total asset visibility as the capability to provide timely and accurate information on the location, movement, status or condition, and identify of units, personnel, equipment, and supplies DOD-wide and having the capability to act on that information.

the FIAR Plan does not identify or outline the department's and/or key components' current financial management weaknesses and capabilities in a manner that would facilitate, among other things, (1) a clear understanding of needed improvements in DOD's or a component's policies, processes and controls, systems and data, and human capital that are needed to address these weaknesses and achieve the FIAR Plan's goals; (2) identification of gaps in planned corrective actions; and (3) establishment of a realistically attainable date, by component and at the department level, for achieving financial statement auditability. The lack of a clear baseline has an adverse impact on the ability of DOD management and other oversight bodies, such as Office of Management and Budget (OMB) and the Congress, to understand the status of improvement efforts and what additional actions are needed.

Linkages between FIAR Plan Goals and Corrective Actions and Reported Accomplishments Are Not Always Clear

The FIAR Plan does not establish linkages between its goals and the corrective actions and accomplishments reported in the plan. Specifically, it does not clearly define how corrective actions or accomplishments identified in the plan contribute individually or collectively within a component or at the department level to address a defined weakness, provide a financial management capability, or achieve a FIAR goal. Without better integration of FIAR Plan goals and corrective actions and reported accomplishments, it will be difficult for DOD management and other oversight bodies to clearly assess the sufficiency of corrective actions and reported accomplishments in addressing the department's financial management weaknesses and achieving financial statement auditability.

Clear Results-Oriented Metrics for Measuring and Reporting Incremental Progress Are Needed

The FIAR Plan does not utilize clear results-oriented metrics to measure and report corrective actions and accomplishments in a manner that clearly demonstrates how they contribute individually or collectively to addressing a defined weakness, providing a certain capability, or achieving a FIAR goal by an estimated milestone date established for each component and the department. For example, many of the corrective actions in the September 2008 FIAR Plan update were reported as 100 percent complete. However, the FIAR Plan provides no description as to how these completed actions contributed individually or collectively to addressing a specific weakness, providing a capability, or achieving a FIAR goal, including what, if any, corrective actions remain. The lack of results-oriented performance measures undermines the department's ability to effectively monitor, measure, and report progress and hold responsible individuals, offices, or organizations accountable.

Accountability Is Not
Clearly Defined or
Assigned and Resources
Budgeted and Consumed
Are Not Identified

The National Defense Authorization Act for Fiscal Year 2008⁶ established the DOD Chief Management Officer (CMO) and the military service CMO positions responsible for efficient and effective business operations within DOD, including the development of a strategic management plan covering those operations and procedures to monitor its progress. Although the FIAR Plan and component FIPs are intended to improve the effectiveness and efficiency of DOD's financial management operations, the FIAR Plan does not identify and describe the oversight roles and responsibilities of DOD's CMO and military service CMOs will have over the financial improvement efforts occurring within the department. The recent establishment of a CMO within the department and its military services was intended to help foster transformation of the department's business operations, including financial management, through an integrated approach. The integration of the CMO into the FIAR Plan's efforts to transform the department's financial management operations is of particular importance given the need for sustained and focused leadership. Since its establishment in 2005, the FIAR Directorate has been led by five different directors. By not defining the roles and responsibilities of the CMO in achieving the FIAR Plan goals, the department's financial community may not have the executive leadership and authority needed to achieve transformation in related business operations, such as acquisition and logistics, which impact financial management but are not within the operational control of the department's financial management community.

Additionally, the FIAR Plan also does not assign accountability for achieving results to specific offices or organizations within the department, such as the Property and Equipment Policy Office within the Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics and/or at lower levels within a DOD component, such as the Deputy Chief of Staff for Logistics, Installations, and Mission Support within the Air Force. Further, the FIAR Plan does not identify and report on the resources budgeted and utilized to achieve a specific corrective action, incremental result, capability, or a FIAR Plan goal. Without formally assigning accountability for results to specific offices and organizations within the department and understanding the cost of improvement efforts, DOD lacks assurance that sufficient and sustainable corrective actions will be taken to address its financial management weaknesses in the most cost-effective manner.

⁶Pub. L. No. 110-181, §904, 122 Stat. 3, 273 (Jan. 28, 2008).

Recent FIAR Directorate Actions

The Acting FIAR Director acknowledged that the FIAR Plan does not yet provide the department with a strategic plan or approach, including a sequence of key activities and their dependencies, for addressing DOD's financial management weaknesses and achieving financial statement auditability. To its credit, the FIAR Directorate is currently in the process of making improvements to the FIAR Plan and component FIPs that it believes will collectively begin to address many of the issues we have identified above. However, the Acting FIAR Director stated that this will be a long-term effort and its effects on the FIAR Plan will be gradual. According to the Acting FIAR Director, the goals of these recent actions are to (1) elevate the level of understanding within the department and its components of the actions needed to identify and address financial management weaknesses, and achieve and sustain financial statement auditability; (2) improve standardization and completeness of FIP activities in identifying and addressing financial management weaknesses; (3) aid in defining the sequence of key activities and their dependencies at the component level, so that the critical path for achieving financial statement auditability can also be defined at the department level; and (4) enhance the FIAR Directorate's ability to guide, monitor, and report on improvement efforts and incremental progress.

Conclusions

The FIAR Plan is intended to provide DOD components with a strategic plan for addressing the department's financial management weaknesses and achieving clean financial statement audit opinions. Additionally, the FIAR Plan is intended to provide DOD management, OMB, and the Congress with an overview of the department's financial management improvement efforts and incremental progress toward addressing DOD's financial management weaknesses and achieving financial statement auditability by estimated milestone dates established for each component and the department. As acknowledged by the department, the FIAR Plan does not yet provide the department or its components with clear and consistent guidance for implementing, measuring, and sustaining corrective actions, and reporting incremental progress toward achieving the FIAR Plan's goals. Additionally, specificity is needed in the FIAR Plan regarding guidance, metrics, linkage of corrective actions and accomplishments to goals, accountability, resources, and governance to enhance the ability of the FIAR Directorate to guide, monitor, and report on the department's efforts to address its financial management weaknesses and achieve financial statement auditability.

To its credit, the FIAR Directorate has initiated actions, consistent with several of our recommendations, to improve the FIAR Plan through its

efforts to (1) standardize component-level FIPs and (2) identify and address gaps in corrective actions planned at the component level and improve progress reporting. However, this will be a long-term effort and its effects on the FIAR Plan will be gradual. These actions are an important step toward enhancing the FIAR Plan as a strategic and management tool for improving oversight of corrective actions and the FIAR Directorate's ability to report on incremental progress to DOD management, OMB, and the Congress. Because the component FIPs provide the detailed steps that feed into the FIAR Plan, it is critical for the FIAR Directorate to have effective management oversight and monitoring and to ensure reliable reporting of the components' financial management improvement efforts. Given the importance of financial management to the department's business operations, the DOD and military service CMOs should have defined roles and responsibilities in overseeing and monitoring financial management improvement efforts.

Recommendations for Executive Action

To increase the FIAR Plan's effectiveness as a strategic and management tool for guiding, monitoring, and reporting on financial management improvement efforts and increasing the likelihood of meeting the department's goal of financial statement auditability, we recommend that the Secretary of Defense direct the DOD CMO to ensure that the military service CMOs and the DOD Comptroller's Acting FIAR Director work jointly, as appropriate, to take the following six actions:

1. Issue guidance to standardize the development of the FIPs, including their format and frequency, to aid in ensuring the
 - sufficiency of corrective actions through the identification of performance gaps in corrective actions planned within and between components;
 - sharing of successful methodologies developed and implemented to address a financial management weakness or achieve a defined capability; and
 - reliability of progress reporting, including clear linkages and descriptions of how the corrective action, individually or collectively contributes to achievement of a defined capability or goal by an estimated milestone date established for each component and the department.
2. Establish a baseline of financial management capabilities and weaknesses at the component level, and ultimately at the department level, that can be used to

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- obtain a clear understanding of needed improvements in DOD's or a component's policies, processes and controls, systems and data, and human capital that are needed to address these weaknesses and support relevant management assertions (i.e., existence or occurrence, completeness, valuation, rights and obligations, and presentation and disclosure) regarding the reliability of reported financial information;
 - identify gaps in planned corrective actions; and
 - establish a realistically attainable date, by component and at the department level, for achieving financial statement auditability.
3. Establish clear results-oriented metrics within the FIAR Plan and component FIPs for measuring and reporting quantifiable incremental results toward achieving defined financial management capabilities, addressing a specific weakness, and/or achieving FIAR Plan goals by an estimated milestone date established for each component and the department.
 4. Describe in the FIAR Plan the oversight roles and responsibilities, if any, of the DOD CMO and military service CMOs over FIAR Plan and FIP improvement efforts, as appropriate.
 5. Assign accountability in the FIAR Plan for achieving results to specific offices or organizations
 - within the department, such as the Property and Equipment Policy Office within the Office of the Under Secretary of Defense (Acquisition, Technology, and Logistics); and/or
 - at lower levels within a DOD component, such as the Deputy Chief of Staff for Logistics, Installations, and Mission Support within the Air Force.
 6. Provide visibility to DOD management and the Congress, within each FIAR Plan update, of resources budgeted and spent to address a specific weakness or achieve specific incremental improvements in the department's financial management capabilities.

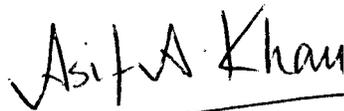
Agency Comments and Our Evaluation

We provided a draft of this report to the Secretary of Defense and received written comments from the Under Secretary of Defense (Comptroller), which are reprinted in appendix II. Overall, DOD concurred with our recommendations and identified specific actions that are either completed, underway, or planned.

DOD acknowledged the importance of properly allocating and utilizing resources to address financial management weaknesses. The department

indicated that it has modified the component level financial improvement plans to begin collecting resource information, but indicated that it may be cost prohibitive to identify and track resources related to addressing specific weaknesses. Given the finite resources available for financial management improvement, we believe that it is incumbent upon the department to identify and use cost information where practical in authorizing and prioritizing corrective actions to ensure that the department's limited business transformation resources are targeted at those actions that will result in long-term sustained financial management improvements.

We are sending copies of this report to the subcommittee. We are also sending copies of this report to the Secretary of Defense, the Deputy Secretary of Defense / Chief Management Officer, the Under Secretary of Defense (Comptroller) / Chief Financial Officer, the Under Secretary of the Army / Chief Management Officer, the Under Secretary of the Navy / Chief Management Officer, the Under Secretary of the Air Force / Chief Management Officer, and OMB's Office of Federal Financial Management. This report is available at no charge on GAO's Web site at <http://www.gao.gov>. Should you or your staff have any questions concerning this report, please contact me at (202) 512-9095 or khana@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Key contributors to this report were Evelyn Logue, Assistant Director; Darby Smith, Assistant Director; F. Abe Dymond, Assistant General Counsel; Richard Cambosos; Jamie Haynes; and Lauren Catchpole.



Asif A. Khan
Director
Financial Management and Assurance

List of Congressional Requesters

The Honorable Thomas R. Carper
Chairman

The Honorable John McCain
Acting Ranking Member
Subcommittee on Federal Financial Management, Government
Information, Federal Services, and International Security
Committee on Homeland Security and Governmental Affairs
United States Senate

The Honorable George V. Voinovich
Acting Ranking Member
Subcommittee on Oversight of Government Management, the Federal
Workforce, and the District of Columbia
Committee on Homeland Security and Governmental Affairs
United States Senate

The Honorable Tom Coburn, M.D.
United States Senate

Appendix I: Briefing Slides from the March 11, 2009, and March 27, 2009, Briefing to the Senate Homeland Security and Governmental Affairs Staff



Financial Management: Achieving Financial Statement Auditability in the Department of Defense

Briefing to Congressional Requesters
March 11, 2009, and March 27, 2009

[Updated April 24, 2009]



Briefing Agenda

- Introduction
 - Objective
 - Summary of Findings
 - Background
 - Findings
 - Conclusions
 - Recommendations
 - Agency Comments and Our Evaluation
 - Scope and Methodology
-



Introduction

- Since the first financial statement audit was attempted at a major Department of Defense (DOD) component over 20 years ago, GAO and DOD auditors have continued to report significant weaknesses in DOD's ability to provide timely, reliable, consistent, and accurate information for management analysis, decision-making, and reporting.
- DOD has undertaken a number of initiatives over the years, such as the Financial Improvement Initiative in 2003, to improve the department's business operations, including financial management, and achieve clean financial statement audit opinions. However, these initiatives have met with limited success.



Introduction (cont'd)

- In 2005, the DOD Comptroller established the DOD Financial Improvement and Audit Readiness (FIAR) Directorate to manage DOD-wide financial improvement efforts and to integrate those efforts with transformation activities, such as those outlined in the department's Enterprise Transition Plan, across the department. DOD considers the Enterprise Transition Plan its department-wide plan for business transformation.
- The FIAR Directorate is responsible for preparing the FIAR Plan to comply with provisions in the National Defense Authorization Act (NDAA) for Fiscal Year 2002 and subsequent provisions in the Authorization Acts for fiscal years 2006 and 2007.



Introduction (cont'd)

- The FIAR Plan is the department's strategic plan and management tool for guiding, monitoring, and reporting on the department's financial management improvement efforts and communicating incremental progress in addressing its financial management weaknesses and achieving financial statement auditability. The plan is updated and provided to DOD management, the Office of Management and Budget (OMB), and the Congress twice a year.



Introduction (cont'd)

- The plan has three main goals: (1) provide timely, reliable, accurate, and relevant financial information; (2) sustain improvements through an effective internal control program;¹ and (3) achieve unqualified (clean) audit opinions on DOD's financial statements.
- To achieve its goals, the FIAR Plan utilizes a bottom-up approach in which DOD components are responsible for developing and implementing component-level financial improvement plans (FIP) to identify and address their financial management weaknesses through sustained improvements and achieve financial statement auditability. The components report accomplishments and progress against planned corrective actions to the FIAR Directorate for reporting in the FIAR Plan.

¹In its annual financial report for fiscal year 2008, DOD reported that it intends to leverage its FIAR Plan to implement the internal control assessment and corrective actions required under OMB Circular No. A-123, *Management's Responsibility for Internal Control*, Appendix A, *Internal Control Over Financial Reporting*.



Objective

- The Chairman, Acting Ranking Member, and Former Ranking Member on Federal Financial Management, Government Information, Federal Services, and International Security, and the Acting Ranking Member, Subcommittee on Oversight of Government Management, the Federal Workforce and the District of Columbia, Senate Committee on Homeland Security and Governmental Affairs, requested GAO analyze the department's FIAR Plan to identify any areas where improvements are needed to enhance the plan's effectiveness as a management tool for guiding, monitoring, and reporting on the department's efforts to identify and resolve its financial management weaknesses and achieve financial statement auditability.
- Our audit scope and methodology are presented at the end of this briefing.



Summary of Findings

- The FIAR Plan identifies three main goals for improving DOD financial information and achieving audit readiness. However, as a strategic plan for addressing DOD's financial management weaknesses and achieving financial statement auditability, we found that the FIAR Plan does not
 - provide clear guidance to DOD components for developing and implementing improvement efforts;
 - establish a baseline of the department's financial management weaknesses and capabilities against which incremental progress toward achieving an estimated milestone date established for each component and the department can be measured;



Summary of Findings (cont'd)

- establish linkages between FIAR Plan goals and the corrective actions and accomplishments reported in the plan;
- utilize clear results-oriented metrics to measure and report corrective actions and accomplishments in a manner that clearly demonstrates how they contribute, individually or collectively, toward addressing a defined weakness, providing a certain capability, or achieving a FIAR goal by an estimated milestone date established for each component and the department;
- describe the oversight roles and responsibilities of the DOD Chief Management Officer (CMO) and military service CMOs over the FIAR Plan and FIP improvement efforts, as appropriate;



Summary of Findings (cont'd)

- assign accountability for achieving results to specific offices or organizations within
 - the department, such as the Property and Equipment Policy Office with the Under Secretary of Defense for Acquisition, Technology, and Logistics and/or
 - at lower levels within a DOD component, such as the Deputy Chief of Staff for Logistics, Installations, and Mission Support within the Air Force; and
- identify and report on the resources budgeted and utilized to achieve a specific corrective action, incremental result, capability, or FIAR Plan goal.
- The Acting FIAR Director acknowledged that the FIAR Plan does not yet provide the department with a strategic plan or approach, including a sequence of key activities and their dependencies, for addressing DOD's financial management weaknesses and achieving financial statement auditability.



Summary of Findings (cont'd)

- To its credit, the FIAR Directorate is currently in the process of making improvements to the FIAR Plan and component FIPs that it believes will collectively begin to address many of the issues we have identified above. However, the Acting FIAR Director stated that this will be a long-term effort and its effect on the FIAR Plan will be gradual. According to the Acting FIAR Director, the FIAR Directorate's objective is to
 - improve standardization and completeness of FIP activities in identifying and addressing financial management weaknesses;
 - aid in defining the sequence of key activities and their dependencies at the component level, so that the critical path for achieving financial statement auditability can also be defined at the department level; and
 - enhance the FIAR Directorate's ability to guide, monitor, and report on improvement efforts and incremental progress.



Background

- DOD's financial management and related business operations and systems problems are pervasive, complex, long-standing, and challenging to resolve.
- The nature and severity of DOD's financial management problems adversely affect the department's ability to
 - control costs, ensure basic accountability over its tangible assets and other resources, anticipate future costs and claims on the budget, measure performance, maintain funds control, prevent fraud, and address pressing management issues, including supporting the warfighters and their families; and
 - obtain clean financial statement audit opinions.



Background (cont'd)

- To draw attention to the need to address these weaknesses, GAO designated DOD financial management and business systems modernization (a key element to successful financial management transformation) as high-risk areas in 1995. DOD's approach to business transformation was added to the high-risk list in 2005. These areas remain on GAO's high-risk list today.²
- In 2003, DOD began the Financial Improvement Initiative (the department's predecessor to its FIAR effort) with the goal of achieving a DOD-wide unqualified (clean) audit opinion on its fiscal year 2007 financial statements.

²GAO, *High-Risk Series: An Update*, GAO-09-271 (Washington, D.C.: January 2009).



Background (cont'd)

- In 2004, we reported that DOD's Financial Improvement Initiative lacked a clear and realistic plan to make its 2007 unqualified audit opinion goal a reality.³ Key issues identified included
 - the absence of a comprehensive, integrated plan or strategy with key milestones, measures/metrics, accountability mechanisms, or cost estimates;
 - limited linkage between component efforts and ongoing business transformation efforts, such as the department's Enterprise Transition Plan; and
 - the absence of management oversight/monitoring structures and processes to ensure component efforts resulted in sustained progress.

³GAO, *Financial Management: Further Actions Are Needed to Establish Framework to Guide Audit Opinion and Business Management Improvement Efforts at DOD*, GAO-04-910R (Washington, D.C.: Sept. 20, 2004).



Background (cont'd)

Key Legislation

- Various statutes⁴ require the department to
 - improve its financial management systems, processes, and controls to ensure that complete, reliable, consistent, and timely information is prepared and responsive to the financial information needs of agency management and oversight bodies, and
 - prepare and issue audited financial statements.

⁴These statutes include the Chief Financial Officers Act, the Government Management Reform Act of 1994, the Federal Financial Management Improvement Act of 1996, and various annual authorization and appropriations act provisions.



Background (cont'd)

Key Legislation—Fiscal Year 2002 NDAA, Section 1008

- Section 1008 of the NDAA for Fiscal Year 2002 requires DOD to minimize resources to develop, compile, report, and audit unreliable financial statements.
- Section 1008 also states that when DOD is able to certify to the DOD Inspector General (IG) that a financial statement for a fiscal year is reliable, DOD may expend resources to develop, compile, report, and audit the statement and the statements of subsequent fiscal years.
- Pursuant to the requirements in section 1008 of the NDAA for Fiscal Year 2002, DOD has asserted in its annual report for the last 7 years that the department is unable to provide adequate evidence supporting material amounts in its financial statements.



Background (cont'd)

Key Legislation—Fiscal Year 2002 NDAA, Section 1008

- Section 1008 of the Fiscal Year 2002 NDAA also requires DOD to submit an annual report⁵ to defense committees, OMB, the Department of the Treasury (Treasury), GAO, and the DOD IG
 - (1) concluding on whether DOD policies, procedures, and systems support financial statement reliability, and the expected reliability of each DOD financial statement; and
 - (2) summarizing specific sections of the annual financial management plan (the FIAR Plan) that
 - (a) detail the priorities, milestones, and measures of success that apply to the preparation of the financial statements,
 - (b) detail the planned improvements in process that are to be implemented within 12 months after the date of the report, and
 - (c) provide an estimate of when each financial statement will convey reliable information.

⁵The Annual Report on Reliability.



Background (cont'd)

Key Legislation—Fiscal Year 2006 NDAA, Section 376

- Section 376 of the NDAA for Fiscal Year 2006
 - Limited DOD's authority to obligate or expend any funds for the purpose of any financial improvement activity related to the preparation, processing, or audit of financial statements until the Secretary submits to congressional defense committees a comprehensive and integrated financial management improvement plan (the FIAR Plan) that
 - describes specific actions to be taken to correct financial management deficiencies that impair the ability of the DOD to prepare timely, reliable, and complete financial information; and
 - systematically ties such actions to process and control improvements and business system modernization efforts described in the business enterprise architecture⁶ and enterprise transition plan required by 10 U.S.C. § 2222.

⁶An enterprise architecture is a modernization blueprint of an organization or a functional or mission area that together with an enterprise transition plan, provides a road map for moving between the current state of operations to the intended state.



Background (cont'd)

Key Legislation—FY 2006 NDAA, Section 376 (cont'd)

- Further, section 376 requires that the Secretary of Defense provide a written determination that each of the financial management improvement activities undertaken is
 - consistent with the financial improvement plan submitted; and
 - likely to improve internal controls or otherwise result in sustained improvements in the ability of the department to produce timely, reliable, and complete financial management information.
- Exception: The limitation regarding the authority to obligate or expend funds does not apply to activities directed at assessing the adequacy of internal controls and remediating any inadequacy identified pursuant to such an assessment.
- DOD has provided FIAR Plan updates to the defense committees and OMB to comply with the requirements of these and subsequent NDAA provisions.



Findings—Clear Guidance Is Needed in Developing and Implementing Improvement Efforts

- Although DOD's September 2008 FIAR Plan emphasizes the importance of activities to identify and correct the department's financial management weaknesses and achieve financial statement auditability, improved clarity is needed to ensure that management assertions regarding the reliability of reported financial information are adequately supported.
- We found that the FIAR Plan does not provide clear guidance to the DOD components for developing and implementing consistent and compatible FIPs. For example, while the FIAR Plan provides examples of the types of activities that should occur within DOD components to identify financial management weaknesses, it is unclear
 - which specific office or organization within an entity is accountable for performing these activities or tasks, particularly in situations where a policy, process and control, or system that should be examined is controlled at the department level and is not within a component's control to change, and
 - what process or methodology a component should apply to identify and coordinate FIP efforts with those of other on-going transformation efforts within the department or a component such as efforts to achieve total asset visibility.⁷

⁷DOD defines total asset visibility as the capability to provide timely and accurate information on the location, movement, status or condition, and identity of units, personnel, equipment, and supplies DOD-wide and having the capability to act on that information.



Findings—Clear Guidance Is Needed in Developing and Implementing Improvement Efforts (cont'd)

- Moreover, our interviews with FIAR Directorate and military service FIP personnel found that the department and its components lack a clear and consistent understanding of how
 - key elements, such as policies, processes and controls, systems and data, and human capital of a component's financial management operations should be assessed to identify weaknesses,⁸ and
 - these key elements contribute individually and/or collectively in providing the audit evidence needed to support management assertions (including existence or occurrence, completeness, valuation, rights and obligations, and presentation and disclosure) regarding the reliability of financial information.

⁸OMB Circular No. A-123, section IV and appendix A requires DOD to assess these key elements and to provide guidance on how to identify and assess weaknesses.



Findings—Clear Guidance Is Needed in Developing and Implementing Improvement Efforts (cont'd)

- Based upon our review of the FIAR Plan, it appears that clearer guidance is needed to aid both component and department-level personnel in ensuring the adequacy and sufficiency of corrective actions taken in supporting management assertions regarding reported financial information.
- Various FIAR Plan updates have reported that certain component line items have achieved audit readiness and were approved for audit by component management and the FIAR Directorate. However, subsequent efforts to validate management's assertions indicated that approval was not warranted and audit readiness would not be achieved until a much later time.
- According to the Acting FIAR Director, the department is increasing its role in assessing the adequacy of a component's basis for asserting audit readiness prior to approving resources to validate a component's audit readiness.



Findings—Clear Guidance Is Needed in Developing and Implementing Improvement Efforts (cont'd)

- For example, in its June and September 2006 FIAR Plans, the FIAR Directorate reported the following accomplishment: “Air Force had corrected its financial deficiencies for Fund Balance with Treasury (General Fund) and has been approved for audit.”
- However, it was subsequently determined that the Air Force did not fully consider all the associated requirements for asserting to the reliability of its Fund Balance with Treasury (General Fund) line item. According to the Acting FIAR Director, the Air Force has developed a plan to begin addressing these weaknesses. In the department’s September 2008 FIAR Plan, DOD reported that Air Force’s Fund Balance with Treasury account will not achieve audit readiness until 2013.



Findings—Clear Guidance Is Needed in Developing and Implementing Improvement Efforts (cont'd)

- Additionally, the June 2007 FIAR Plan reported that DOD’s “military equipment baseline valuations were correct, that all military equipment that should be capitalized has been valued, and that DOD owns and has rights to all capitalized military equipment.” This assertion was made despite several sources of information, including an internal verification and validation study⁹ and DOD auditor reports,¹⁰ which contradicted the basis for this assertion, including the department’s ability to sustain its baseline valuation.

⁹Department of Defense, Property and Equipment Policy, Office of the Undersecretary of Defense for Acquisition, Technology, and Logistics, *Internal Validation and Verification Project: Military Equipment Valuation* (June 13, 2006).

¹⁰Department of Defense Inspector General, *Financial Management: Report on Development of the DOD Baseline for Military Equipment*, D-2005-114 (Arlington, VA: Sept. 30, 2005); and *Financial Management: Report on the Review of the Development of the DOD Baseline for Military Equipment*, D-2005-112 (Arlington, VA: Sept. 30, 2005); Air Force Audit Agency, *Air Force Military Equipment Baseline Valuation*, F2007-0009-FB3000 (May 29, 2007); and *Military Equipment Baseline—Electronic Pods*, F2007-0003-FB3000 (Jan. 19, 2007).



Findings—Clear Guidance Is Needed in Developing and Implementing Improvement Efforts (cont'd)

- Efforts are currently under way at the component level to address the shortcomings in the department's initial efforts to establish and sustain a military equipment valuation baseline.
- Current estimates in the September 2008 FIAR Plan state that auditability of military equipment will be achieved in 2014 for the Army and the Navy and in 2016 for the Air Force.



Findings—No Clear Baseline Exists against Which Incremental Progress Can Be Measured

- The FIAR Plan does not establish a baseline of the department's and/or key components' current financial management weaknesses and capabilities in a manner that would facilitate
 - a clear understanding of needed improvements in DOD's or a component's policies, processes and controls, systems and data, and human capital that are needed to address these weaknesses and achieve the FIAR Plan's goals;
 - identification of gaps in planned corrective actions; and
 - establishment of a realistically attainable date, by component and at the department level, for achieving financial statement auditability.
- Congressional and OMB staff have expressed frustration with the FIAR plan's lack of a baseline from which to assess incremental progress.



Findings—Linkages between FIAR Plan Goals and Corrective Actions and Reported Accomplishments Are Not Always Clear

- The FIAR Plan does not establish linkages between its goals and the corrective actions and accomplishments reported in the plan. Specifically, it does not clearly define how corrective actions or accomplishments identified in the plan contribute individually or collectively within a component or at the department level to addressing a defined weakness, providing a financial management capability, or achieving a FIAR goal. The lack of clear linkage makes it difficult to clearly assess the sufficiency of corrective actions and reported accomplishments in addressing DOD's financial management weaknesses and achieving financial statement auditability.
 - For example, the September 2008 FIAR Plan identifies a number of accomplishments related to its efforts to improve visibility into Global War on Terror (GWOT) funds appropriated, payments made, and remaining funds available.
 - However, the plan provides no discussion as to whether and how its efforts to improve GWOT funds accountability contribute in a broader sense to improved funds control DOD-wide and incremental progress toward achieving financial statement auditability.



Findings—Clear Results-Oriented Metrics for Measuring and Reporting Incremental Progress Are Needed

- The FIAR Plan does not utilize clear results-oriented metrics to measure and report corrective actions and accomplishments in a manner that clearly demonstrates how they contribute individually or collectively to addressing a defined weakness, providing a certain capability, or achieving a FIAR goal by an estimated milestone date established for each component and the department. Furthermore, the FIAR Plan does not identify task dependencies—key to identifying corrective actions/tasks that must be finished on schedule if the planned result, capability, or goal is to be achieved as planned. For example, the September 2008 FIAR Plan update reported or identified
 - that DOD would complete its efforts to establish an interface between the department's item unique identification (IUID) registry and its military equipment accountability system to automate updates for Navy small craft by December 31, 2008, but provided no measure of incremental progress toward achieving this milestone;



Findings—Clear Results Oriented Metrics for Measuring and Reporting Incremental Progress Are Needed (cont'd)

- that by March 31, 2010, the Air Force would complete the corrective action related to military equipment “Achieve Defense Enterprise Accounting and Management System-DEAMS- initial operational capability,”¹¹ but reported no progress toward achieving this goal, even though the Air Force initiated its effort to acquire DEAMS in August 2003;

¹¹Initial operational capability is achieved when a system is implemented with some minimal capabilities and additional capabilities are planned before the system is determined to be fully operational.



Findings—Clear Results Oriented Metrics for Measuring and Reporting Incremental Progress Are Needed (cont'd)

- no dependency relationship among any of the corrective actions identified for the department or any of its components. For example,
 - the relationship between components' efforts to identify the universe of units, facilities, property, and/or operations that may have environmental liabilities and their corrective actions planned to document that all property, plant, and equipment records have been reviewed and the liabilities properly recorded is unclear; and
 - the Air Force Audit Agency had completed a review of capital lease reporting, but the component did not identify whether or how the audit results affected its planned corrective actions.



Findings—Clear Results-Oriented Metrics for Measuring and Reporting Incremental Progress Are Needed (cont'd)

- Many of the corrective actions in the September 2008 FIAR Plan update were reported as 100 percent complete. However, the FIAR Plan provides no description as to how these completed actions contributed individually or collectively toward addressing a specific weakness, providing a capability, or achieving a FIAR goal by an estimated milestone date established for each component and the department and what corrective actions remain.
- The lack of clear, results-oriented performance measures undermines the department's ability to effectively monitor, measure, and report progress or hold responsible individuals, offices, or organizations accountable for results.



Findings—Roles and Responsibilities of the CMOs Are Not Defined

- The NDAA for Fiscal Year 2008 established the DOD CMO and military service CMO positions responsible for efficient and effective business operations within DOD, including the development of a strategic management plan covering those operations and procedures to monitor its progress.¹²
- Although the FIAR Plan and component FIPs are intended to improve the effectiveness and efficiency of DOD's financial management operations, the FIAR Plan does not identify or describe the roles and responsibilities
 - the CMO will have in overseeing and monitoring the FIAR Plan and DOD's financial improvement efforts. This is particularly important given the need for sustained and focused leadership. Since its establishment in 2005, the FIAR Directorate has been led by five different directors;
 - the military service CMOs will have in overseeing and monitoring their components' financial improvement efforts.

¹²Pub. L. No. 110-181, §904, 122 Stat. 3, 273 (Jan. 28, 2008).



Findings—Roles and Responsibilities of the CMOs Are Not Defined (cont'd)

- The recent establishment of a CMO within the department and its military services was intended to help foster transformation of the department's business operations, including financial management through an integrated approach.
- By not defining the roles and responsibilities of the CMO in achieving financial management transformation, the department may not have the executive leadership and authority needed to influence transformation in related business operations, such as acquisition and logistics, that impact financial management, but are not within the operational control of the department's financial management community.



Findings—Accountability Is Not Assigned to Specific Offices or Organizations

- The FIAR Plan does not assign accountability for achieving results to specific offices or organizations within
 - the department, such as the Property and Equipment Policy Office within the Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics, and/or
 - at lower levels within a DOD component, such as the Deputy Chief of Staff for Logistics, Installations, and Mission Support within the Air Force.
- Without formally assigning accountability for results, DOD lacks assurance that sufficient and sustainable corrective actions will be taken to address its financial management weaknesses and achieve financial statement auditability.



Findings—Resources Budgeted and Consumed Are Not Identified

- The FIAR Plan does not identify at the department level and/or at the component level, as appropriate, the resources budgeted and consumed to achieve a specific corrective action, financial management capability, or FIAR Plan goals.
 - As a result, DOD lacks assurance that resources utilized for corrective actions are directed in the most efficient and cost effective manner.
-



Findings—Recent FIAR Directorate Actions

- The Acting FIAR Director acknowledged that the FIAR Plan does not yet provide the department with a strategic plan or approach, including a sequence of key activities and their dependencies, for addressing DOD's financial management weaknesses and achieving financial statement auditability. To its credit, the FIAR Directorate is currently in the process of making improvements to the FIAR Plan and component FIPs that it believes will collectively begin to address many of the issues we have identified above. However, the Acting FIAR Director stated that this will be a long-term effort and its effects on the FIAR Plan will be gradual.
- According to the Acting FIAR Director, the goals of these recent actions are to
 - elevate the level of understanding within the department and its components of the actions needed to identify and address financial management weaknesses, and achieve and sustain financial statement auditability;



Findings—Recent FIAR Directorate Actions (cont'd)

- improve standardization and completeness of FIP activities in identifying and addressing financial management weaknesses;
 - aid in defining the sequence of key activities and their dependencies at the component level, so the critical path for achieving financial statement auditability can also be defined at the department level; and
 - enhance the FIAR Directorate's ability to guide, monitor, and report on improvement efforts and incremental progress.
-



Findings—Recent FIAR Directorate Actions (cont'd)

- To improve its strategic approach, the FIAR Directorate is in the process of
 1. developing and mandating the use of a standard FIP template to aid in
 - providing greater comparability of corrective actions/approaches planned among components for addressing similar issues to ensure completeness of corrective actions;
 - ensuring that weaknesses within the department's policies, processes and controls, and systems and data, are identified and addressed in a manner, which provides management with a greater level of assurance that the conditions that may cause an account balance to be misstated—missing entries, erroneous entries, or that are incorrectly presented and described in the financial statements—are addressed;



Findings—Recent FIAR Directorate Actions (cont'd)

- identifying specific results/progress toward addressing deficiencies and achieving financial statement auditability;
 - identifying the sequence of key activities and their dependencies for achieving financial statement auditability at the component level, which is needed to determine the critical path at the department level and ultimately, when component and departmentwide financial statements are likely to be auditable; and
 - assigning accountability and identifying resource needs for achieving corrective actions.
-



Findings—Recent FIAR Directorate Actions (cont'd)

2. establishing a task force of personnel from the military services, the FIAR Directorate, and the DOD IG (as an independent observer/advisor) to begin reviewing component approaches directed at identifying and correcting financial management weaknesses and achieving auditability.
 - DOD intends to focus its efforts initially on the Army's FIP efforts related to fund balance with Treasury and the Navy's FIP efforts related to real property to identify weaknesses and gaps in their current approaches.



Findings—Recent FIAR Directorate Actions (cont'd)

- The components will be required to prepare and implement corrective action plans and update their FIPs to remediate weaknesses identified by the task force.
- The task force expects to complete these initial reviews by September 2009.
- According to the Acting FIAR Director, DOD hopes to use these task force reviews to (1) identify and share areas where the FIP approach can be improved and (2) develop a methodology that can be applied to future reviews of other component financial management improvement areas.



Conclusions

- The FIAR Plan is intended to provide DOD components with a strategic plan for addressing the department's financial management weaknesses and achieving clean financial statement audit opinions. Additionally, the FIAR Plan is intended to provide DOD management, OMB, and the Congress with an overview of the department's financial management improvement efforts and the incremental progress these efforts are making toward addressing DOD's financial management weaknesses and achieving financial statement auditability by estimated milestone dates established for each component and the department.
- As acknowledged by the department, the FIAR Plan does not yet provide the department or its components with clear and consistent guidance for implementing, measuring, and sustaining corrective actions and reporting incremental progress toward achieving the FIAR Plan's goals.



Conclusions (cont'd)

- Additional specificity is needed in the FIAR Plan regarding guidance, metrics, linkage of corrective actions and accomplishments to goals, accountability, resources, and governance to enhance the ability of the FIAR Directorate to guide, monitor, and report on the department's efforts to address its financial management weaknesses and achieve financial statement auditability.
- To its credit, the FIAR Directorate has initiated actions, consistent with several of our recommendations, to improve the FIAR Plan through its efforts to (1) standardize component level FIPs and (2) identify and address gaps in corrective actions planned at the component level and improve progress reporting. However, this will be a long-term effort and its effects on the FIAR Plan will be gradual.



Conclusions (cont'd)

- These actions are an important step toward enhancing the FIAR Plan as a strategic and management tool for improving oversight of corrective actions and the FIAR Directorate's ability to report on incremental progress to DOD management, OMB, and the Congress.
 - Because the component FIPs provide the detailed steps that feed into the FIAR Plan, it is critical for the FIAR Directorate to have effective management oversight and monitoring and to ensure reliable reporting of the components' financial management improvement efforts.
 - Given the importance of financial management to the department's business operations, the department and military service CMOs should have defined roles and responsibilities in overseeing and monitoring financial management improvement efforts.
-



Recommendations for Executive Action

- To increase the FIAR Plan's effectiveness as a strategic and management tool for guiding, monitoring, and reporting financial management improvement efforts and increasing the likelihood of meeting the department's goal of financial statement auditability, we recommend that the Secretary of Defense direct the DOD CMO to ensure that the military service CMOs and the DOD Comptroller's Acting FIAR Director work jointly, as appropriate, to take the following six actions:



Recommendations for Executive Action (cont'd)

1. Issue guidance to standardize the development of the FIPs, including their format and frequency, to aid in ensuring the
 - sufficiency of corrective actions through the identification of performance gaps in corrective actions planned within and between components;
 - sharing of successful methodologies developed and implemented to address a financial management weakness or achieve a defined capability; and
 - reliability of progress reporting, including clear linkages and descriptions of how the corrective action, individually or collectively, contributes to the achievement of a defined capability or goal by an estimated milestone date established for each component and the department.



Recommendations for Executive Actions (cont'd)

2. Establish a baseline of financial management capabilities and weaknesses at the component level, and ultimately at the department level, that can be used to
 - obtain a clear understanding of needed improvements in DOD's or a component's policies, processes and controls, systems and data, and human capital that are needed to address these weaknesses and support relevant management assertions (i.e., existence or occurrence, completeness, valuation, rights and obligations, and presentation and disclosure) regarding the reliability of reported financial information;
 - identify gaps in planned corrective actions; and
 - establish a realistically attainable date, by component and at the department level, for achieving financial statement auditability.



Recommendations for Executive Actions (cont'd)

3. Establish clear results-oriented metrics within the FIAR Plan and component FIPs for measuring and reporting quantifiable incremental results toward achieving defined financial management capabilities, addressing a specific weakness, and/or achieving FIAR Plan goals by an estimated milestone date established for each component and the department.

4. Describe in the FIAR Plan the oversight roles and responsibilities, if any, of the DOD CMO and military service CMOs over FIAR Plan and FIP improvement efforts, as appropriate.



Recommendations for Executive Action (cont'd)

5. Assign accountability in the FIAR Plan for achieving results to specific offices or organizations
 - within the department, such as the Property and Equipment Policy Office within the Office of the Under Secretary of Defense for Acquisition, Technology, and Logistics; and/or
 - at lower levels within a DOD component, such as the Deputy Chief of Staff for Logistics, Installations, and Mission Support within the Air Force.
6. Provide visibility to DOD management, OMB, and the Congress, within each FIAR Plan update, of resources budgeted and spent to address a specific weaknesses or achieve specific incremental improvements in the department's financial management capabilities.



Agency Comments and Our Evaluation

- We provided a draft of this report to the Secretary of Defense and received written comments from the Under Secretary of Defense (Comptroller), which are reprinted in appendix II. Overall, DOD concurred with our recommendations and identified specific actions that are either completed, underway, or planned.



Agency Comments and Our Evaluation (cont'd)

- DOD acknowledged the importance of properly allocating and utilizing resources to address financial management weaknesses. The department indicated that it has modified the component level financial improvement plans to begin collecting resource information, but indicated that it may be cost prohibitive to identify and track resources related to addressing specific weaknesses.
- Given the finite resources available for financial management improvement, we believe that it is incumbent upon the department to identify and use cost information where practical in authorizing and prioritizing corrective actions to ensure that the department's limited business transformation resources are targeted at those actions that will result in long-term sustained financial management improvements.



Scope and Methodology

- We reviewed the DOD FIAR Plans for December 2005 through September 2008 and the FIPs used to prepare the March and September 2008 FIAR updates to obtain an understanding of the
 - process the department has outlined for its components to follow in identifying and correcting their financial management weaknesses and supporting the department's efforts to achieve and sustain financial statement auditability;
 - reported financial management accomplishments;
 - metrics utilized within the plan to assess and report incremental progress;
 - changes, if any, to the department's financial management improvement and audit readiness strategy; and
 - FIAR Directorate's oversight and monitoring of the FIAR Plan, including reported accomplishments and incremental progress.



Scope and Methodology (cont'd)

- To further our understanding of the FIAR Plan and FIPs, we obtained briefings and conducted interviews with key personnel responsible for these plans within the Office of the Under Secretary of Defense (Comptroller), the FIAR Directorate and the Financial Management and Comptroller Offices of the Army, the Navy, and the Air Force.
- We obtained briefings from FIAR Directorate personnel regarding the FIAR Web-based planning tool and reviewed extracts from the tool to further our understanding of the department's measures/metrics, monitoring, and reporting process.



Scope and Methodology (cont'd)

- To assess the adequacy of DOD's FIAR Plan in providing DOD components with a strategy for addressing the department's financial management weaknesses and achieving financial statement auditability, we utilized criteria that identified the key elements of a strategic plan as identified by our previous work¹² and as stipulated by the Government Performance and Results Act of 1993. These elements include
 - providing a comprehensive view of performance, including the establishment of a baseline of current operational functions, capabilities, and performance against which progress toward a defined goal or objective can be measured;
 - aligning of goals and measures with departmentwide goals and cascading goals and measures to lower organizational levels;
 - establishing timelines and demonstrating results;
 - assigning of accountability for achieving results; and
 - linking resource needs to performance.

¹²See GAO, *Defense Business Transformation: Achieving Success Requires a Chief Management Officer to Provide Focus and Sustained Leadership*, GAO-07-1072 (Washington, D.C.: Sept. 5, 2007).



Scope and Methodology (cont'd)

- Given the importance of ensuring the sufficiency of corrective actions and accomplishments in achieving the FIAR Plan goals, we considered the financial statement assertions as criteria in assessing the adequacy of the FIAR Plan as a strategic and management tool for guiding, monitoring, and reporting incremental progress toward identifying and addressing financial management weaknesses and achieving auditability.
 - Assertions are representations by management regarding the reliability of reported financial information. These assertions include: existence or occurrence, completeness, rights and obligations, valuation or allocation, and presentation and disclosure.¹³
 - Most of the auditors' work in forming an opinion on financial statements consists of obtaining and evaluating sufficient appropriate evidence concerning management's assertions in the financial statements.

¹³The American Institute of Certified Public Accountants' Statement on Audit Standards No. 106: Audit Evidence, and the GAO/President's Council on Integrity and Efficiency Financial Audit Manual.



Scope and Methodology (cont'd)

- We performed our review from October 2008 through May 2009 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 based on our audit objectives. We believe the evidence obtained provides a reasonable basis for the our findings and conclusions based on our audit objectives.

Appendix II: Comments from the Under Secretary of Defense (Comptroller)



COMPTROLLER

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

APR 21 2009

Mr. Asif A. Khan
Director, Financial Management and Assurance
U.S. Government Accountability Office
441 G Street, N.W.
Washington, DC 20548

Dear Mr. Khan,

This is the Department of Defense (DoD) response to the GAO draft report GAO-09-373, "FINANCIAL MANAGEMENT: Achieving Financial Statement Auditability in the Department of Defense" (GAO code 197081).

The Department is encouraged that the draft report cites the work that the Financial Improvement and Audit Readiness (FIAR) Directorate has completed to improve the FIAR Plan and the underlying efforts of the Department to achieve its financial improvement objectives. As with any effort the size and scope of the Department's financial management improvement efforts, continuous evaluation and evolution of the strategy and approach is warranted. The FIAR Directorate and the financial management leadership in the Military Services and Defense Agencies remain devoted to achieving the goals of the FIAR Plan in the most efficient manner possible.

The financial management of the Department is the responsibility of the Chief Financial Officer (CFO) acting on behalf of the Secretary of Defense. As in any organization the CFO collaborates with and is dependent on operational organizations to implement and operate effective internal controls to achieve reliable financial management. The Chief Management Officer (CMO) of the Department and the CMOs of the Military Services are critical to the Department's success by facilitating the prioritization of financial management improvement efforts across the functional areas of the Department.

I agree in principle with the recommendations in your draft report so long as responsibility for improvement remains with the CFO. Consistent with that view, and as stated in your report and our detailed responses attached, the FIAR Directorate in my office is already implementing solutions to address them. We value the feedback of the GAO received during the review and in this draft report. We look forward to continued collaboration to ensure that our efforts are as effective as possible.

**Appendix II: Comments from the Under
Secretary of Defense (Comptroller)**

The Department appreciates the opportunity to comment on the draft report. My point of contact for this effort is Ms. Radha Sekar. She can be reached at 703-697-3200 or by email at radha.sekar@osd.mil.

Sincerely,



Robert F. Hale

Attachment:
As stated

GAO DRAFT REPORT DATED MARCH 18, 2009
GAO-09-373 (GAO CODE 197081)

“FINANCIAL MANAGEMENT: ACHIEVING FINANCIAL
STATEMENT AUDITABILITY IN THE DEPARTMENT OF DEFENSE”

DEPARTMENT OF DEFENSE COMMENTS
TO THE GAO RECOMMENDATIONS

RECOMMENDATION 1: The GAO recommends that the Secretary of Defense direct the DoD Chief Management Officer (CMO) to ensure that the military service CMOs and the DoD Comptroller’s Acting Financial Improvement and Audit Readiness (FIAR) Director work jointly, as appropriate, to issue guidance to standardize the development of the financial improvement plans (FIP), including their format and frequency. (Page 7/GAO Draft Report)

DOD RESPONSE: Concur. The Under Secretary of Defense (Comptroller)/Chief Financial Officer (USD(C)) will retain overall responsibility for statement audibility and ensure the Military Services Financial Improvement Plan Program Management Offices and Military Service CMOs collaborate with the FIAR Directorate on implementing standard FIPs. The FIAR Directorate began the effort to establish standard FIP plan content and format in the last quarter of fiscal year 2008. The guidance for standard FIP format and content was delivered to the Components on December 18, 2008. The Components’ FIPs were updated to comply with the new guidance as of February 28, 2009. The FIAR Directorate continues to work with the Components to improve the content of their FIPs and achieve standard formats, contents and outcomes within the Components’ FIPs.

RECOMMENDATION 2: The GAO recommends that the Secretary of Defense direct the DoD Chief Management Officer (CMO) to ensure that the military service CMOs and the DoD Comptroller’s Acting Financial Improvement and Audit Readiness (FIAR) Director work jointly, as appropriate, to establish a baseline of financial management capabilities and weaknesses at the component level, and ultimately at the department level. (Page 7/GAO Draft Report)

DOD RESPONSE: Concur. The USD(C) will ensure the FIAR Directorate works directly with the Military Service Financial Improvement Plan Program Management Offices to establish capability baselines related to financial controls and to ensure that the military services make appropriate progress in achieving the objectives and capabilities.

The FIAR Directorate has already begun collaborating with the Military Services Financial Improvement Plan Program Management Offices to establish a set of control

Attachment
Page 1 of 3

objectives and capabilities that are critical to achieving improved financial management and audit readiness. These objectives and capabilities have been integrated into the Component FIPs to serve as the outcomes against which progress will be measured.

RECOMMENDATION 3: The GAO recommends that the Secretary of Defense direct the DoD Chief Management Officer (CMO) to ensure that the military service CMOs and the DoD Comptroller's Acting Financial Improvement and Audit Readiness (FIAR) Director work jointly, as appropriate, to establish clear results-oriented metrics within the FIAR Plan and components FIPS for measuring and reporting quantifiable incremental results toward achieving defined financial management capabilities, addressing a specific weakness, and/or achieving FIAR Plan goals by an estimated milestone date established for each component and the department. (Page 7/GAO Draft Report)

DOD RESPONSE: Concur. The USD(C) will ensure the Military Service CMOs, the Military Service Financial Improvement Plan Program Management Offices, and the FIAR Directorate will collaborate to establish and implement outcome based performance metrics to measure progress toward financial management improvement and auditability.

As stated in the response to recommendation 2, the FIAR Directorate has already begun collaboration with the Military Services to establish objectives and define the capabilities needed to achieve financial management improvement and audit readiness. These objectives and capabilities will serve as the outcome-oriented metrics and milestones to measure incremental and meaningful progress towards the ultimate goals.

RECOMMENDATION 4: The GAO recommends that the Secretary of Defense direct the DoD Chief Management Officer (CMO) to ensure that the military service CMOs and the DoD Comptroller's Acting Financial Improvement and Audit Readiness (FIAR) Director work jointly, as appropriate, to describe in the FIAR Plan the oversight roles and responsibilities, if any, of the DoD CMO and the military service CMOs over FIAR Plan and FIP improvement efforts as appropriate. (Page 7/GAO Draft Report)

DOD RESPONSE: Concur. The USD(C) will be responsible for implementing this option.

RECOMMENDATION 5: The GAO recommends that the Secretary of Defense direct the DoD Chief Management Officer (CMO) to ensure that the military service CMOs and the DoD Comptroller's Acting Financial Improvement and Audit Readiness (FIAR) Director work jointly, as appropriate, to assign accountability in the FIAR Plan for achieving results to specific offices or organizations. (Page 7/GAO Draft Report)

DOD RESPONSE: Concur. The FIAR Plan already is the responsibility of the Secretary of each Military Service and the Director of the Defense Agencies as they formally coordinate on the FIAR Plan as prepared by their assigned offices in

collaboration with the FIAR Directorate. The USD(C) as the chief financial officer holds the responsibility for achieving auditable financial statements for the Department. The USD(C) will work with the Military Service financial communities and CMOs and Directors of the Defense Agencies and FIAR Directorate on assigning accountability for FIAR progress to the appropriate offices and organizations below the CMO level in the Military Services and Defense Agencies. In order to accommodate this, the FIAR Directorate has added a requirement to the FIPs to identify the specific offices and organizations responsible for achieving each control objective and capability.

RECOMMENDATION 6: The GAO recommends that the Secretary of Defense direct the DoD Chief Management Officer (CMO) to ensure that the military service CMOs and the DoD Comptroller's Acting Financial Improvement and Audit Readiness (FIAR) Director work jointly, as appropriate, to provide visibility to DoD management and the Congress, within each FIAR Plan update, of resources budgeted and spent to address a specific weakness or achieve specific incremental improvements in the department's financial management capabilities. (Page 8/GAO Draft Report)

DOD RESPONSE: Partially concur. The USD(C) will ensure the Military Service CMOs and Military Service Financial Improvement Plan Program Management Offices collaborate with the FIAR Directorate to provide visibility of the resources needed and used for FIAR efforts. The Department recognizes that it is important to properly allocate resources to the FIAR effort and to ensure that once allocated those resources are effective. The FIP plans have been modified to collect this information; however, the cost and effort of assigning and tracking resources to address specific weaknesses may be prohibitive.

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