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**DOD'S PLANS FOR FINANCIAL
MANAGEMENT IMPROVEMENT AND
ACHIEVING AUDIT READINESS**

HEARING

BEFORE THE

PANEL ON DEFENSE FINANCIAL MANAGEMENT
AND AUDITABILITY REFORM

OF THE

COMMITTEE ON ARMED SERVICES
HOUSE OF REPRESENTATIVES

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PANEL ON DEFENSE FINANCIAL MANAGEMENT
AND AUDITABILITY REFORM

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**DOD'S PLANS FOR FINANCIAL MANAGEMENT
IMPROVEMENT AND ACHIEVING AUDIT READINESS**

HOUSE OF REPRESENTATIVES,
COMMITTEE ON ARMED SERVICES,
PANEL ON DEFENSE FINANCIAL MANAGEMENT AND
AUDITABILITY REFORM,
Washington, DC, Thursday, July 28, 2011.

The panel met, pursuant to call, at 8:00 a.m. in room 2118, Rayburn House Office Building, Hon. K. Michael Conaway (chairman of the panel) presiding.

**OPENING STATEMENT OF HON. K. MICHAEL CONAWAY, A
REPRESENTATIVE FROM TEXAS, CHAIRMAN, PANEL ON
DEFENSE FINANCIAL MANAGEMENT AND AUDITABILITY
REFORM**

Mr. CONAWAY. Welcome to the inaugural hearing for the Armed Services Committee's Panel on Defense Financial Management and Auditability Reform.

The panel met to organize on July 13th and had our first informal briefing last week. We have adopted an organizational plan, including a detailed work plan, to assist us in examining the progress the Department of Defense has made in improving financial management and achieving audit readiness and identifying the challenges that remain.

Without objection, I would like to enter the organizational plan into the record for today's hearing.

[The information referred to can be found in the Appendix on page 69.]

Mr. CONAWAY. But more important are the details of our oversight agenda. Chairman McKeon and Ranking Member Smith have charged this body with making recommendations and providing continuity of leadership on this issue.

Therefore, I would like to take a moment to introduce each of the panel members and thank them for their commitment to join Rob and me as we continue to work on the previous Defense Acquisition Panel.

In addition to my partner, Rob Andrews of New Jersey, the following members will serve on the panel: Scott Rigell from Virginia; Joe Courtney from Connecticut; Steven Palazzo of Mississippi; Tim Ryan of Ohio; Todd Young of Indiana.

They will be embarrassed that they weren't here to hear their names read and bragged on, and all that kind of stuff. The first question on the panel's work plan addresses whether DOD's [the Department of Defense's] current financial improvement and audit readiness strategy, methodology and timeliness are appropriate.

I feel this is the appropriate starting point as DOD has initiated numerous efforts over the years to address its financial management weaknesses and achieve audit readiness with little or no success.

In fact, for over 20 years now, GAO [Government Accountability Office] and DOD auditors have continued to report significant weaknesses in DOD's ability to provide timely, reliable and useful information for decisionmaking and reporting.

In these difficult fiscal times it is absolutely crucial that DOD has reliable information to manage its resources. Having reliable information is essential, is especially critical, as DOD attempts to implement the \$178 billion in cuts and efficiencies proposed by the former Secretary of Defense, not to mention how important it is for DOD, it will be, if DOD is forced to look for further significant cuts in the near future.

The Department of Defense also needs to provide assurance to the American taxpayer that they are not wasting resources. However, because of DOD's poor internal controls, the financial management area has been on GAO's list of high-risk programs that are vulnerable to waste, fraud and abuse since 1995.

The Defense Authorization Act of 2010 requires that DOD's financial statements be ready for audit by no later than September 30, 2017.

Today we will hear about DOD's strategy and methodology to get the Department of Defense to audit readiness by 2017 and the challenges that the Department faces to achieving that goal. We do not expect to discuss all the challenges DOD is facing in great detail in this hearing, but it is a good starting point to understanding what the Department is up against in its financial improvement efforts.

I expect the panel to hold future hearings that will cover in much more detail the challenges that the Department is facing in their efforts to resolve the issues.

I would like thank our witnesses in advance for their testimony and agreeing to be here at such an early hour. Our witnesses today are the Honorable Robert Hale, Under Secretary of defense, comptroller; the Honorable Elizabeth McGrath, deputy chief management officer, Department of Defense; Mr. Asif Khan, the director of financial management and assurance at GAO.

I would now like to turn to Rob Andrews for any remarks he would like to make.

Rob.

[The prepared statement of Mr. Conaway can be found in the Appendix on page 29.]

STATEMENT OF HON. ROBERT ANDREWS, A REPRESENTATIVE FROM NEW JERSEY, RANKING MEMBER, PANEL ON DEFENSE FINANCIAL MANAGEMENT AND AUDITABILITY REFORM

Mr. ANDREWS. Well, good morning to my colleagues.

Good morning, ladies and gentleman. We thank you for your attendance at this early hour.

I want to thank Chairman Conaway for his leadership on this panel. It has been a pleasure to work with him the last couple of

years, to roll up our sleeves, and I am very much looking forward to continuing that effort.

And I also wanted to take a minute and introduce Congressman Jim Cooper, who is a member of our full committee, who is the ranking member on the Oversight Committee, who I commend for having the zeal to be here at this hour to participate in this.

You can't make good decisions without good information. And when it comes to the complexity of the Department of Defense, you can't have good information without financial statements. And we don't have them.

Now, most people hear that and think that is the result of some sinister conspiracy to hide money or this or that. That is simply not true. What is true is that the Department of Defense is probably the most complex organization in the world. It is actually multiple organizations under the same organizational rubric.

It does just about everything, and it is organized just about everywhere, so—and it is this *sui generis* organization. You know, the way you value a hotel or a shopping mall is not the way you would value Andrews Air Force Base, a very well-named installation here in the country.

[Laughter.]

So I want to dispel from the outset the notion that the reason we don't have these statements is some military-industrial conspiracy to hide things from the public. That is not true.

What is true are two other things. One is that it is a complex task to figure out how to get from where we are today to where we need to be, which are good, auditable financial statements.

But the second is it is doable. And I think you are going to hear from this panel today that these are folks involved in getting it done. And the briefing we had last week shows that there has been a sincere, concerted, focused effort from Secretary Hale and his team.

And we are anxious to try to be a resource in making that happen so that the members of Congress and the public can make well-informed decisions about future expenditures in this Department.

So I look forward to hearing what the witnesses have to say, and I am glad to join you this morning.

Mr. CONAWAY. Well, thank you. With that, I will turn the microphones over to the panel, whoever wants to start, however you want to do it.

So, Bob.

STATEMENT OF HON. ROBERT F. HALE, UNDER SECRETARY OF DEFENSE (COMPTROLLER), U.S. DEPARTMENT OF DEFENSE

Secretary HALE. Well, good morning, Congressman Conaway, Congressman Andrews, members of the panel. Thank you for the opportunity to testify this morning on financial management improvements at the Department of Defense.

Secretary Leon Panetta, our new Secretary of Defense, shares your interest and mine in improving financial management at DOD and has asked that I provide him a comprehensive review of our

efforts in the near future. And I look forward to getting his personal guidance on this topic.

To bring you up to date on our progress, the Department's Deputy Chief Management Officer, Ms. Beth McGrath, and I have prepared a joint statement, which we have submitted for the record. We will jointly summarize that statement. We are going to do tag-team. I will start out. Beth will join midway on some of the I.T. [Information Technology] system issues, and I will finish up.

I believe that defense financial managers have three broad goals. They need to help the Department acquire the resources necessary to meet national security objectives. It is the key goal, the budget goal, if you will.

Second, they need to ensure that once those resources are enacted, they are spent in a manner that is legal, effective and efficient. And that goal probably encompasses many that we will talk about today.

And, third, they need to champion a strong financial management workforce, because if we don't do that, we won't be able to accomplish the other goals.

The first thing I would like to note is as we work to meet national security objectives, DOD financial management has its strengths. Mainly we are effective, in my view, in meeting the needs of our warfighters—the financial management needs—financial needs of our warfighters. And that is the key goal, maybe the most important one for me.

We also have a dedicated workforce of more than 60,000 financial management professionals, and through personal experience I can tell you they bring a culture of stewardship to their jobs. They worry about whether or not this money is spent effectively.

We also have effective financial processes in some key areas. As a result, violations of key financial laws are few in the Department of Defense. Timely and accurate payments are the rule, and interest associated with late payments is quite low.

Financial managers have also made some progress on the areas that I know of, and an area that I know is of particular interest, I should say, to this panel, namely the financial improvement and audit readiness area.

I am sorry, I am getting ahead of myself. There are some other things that we do that I wanted to cover before I get to the FIAR [Financial Improvement and Audit Readiness] plan.

We are working to try to improve financial information. That is key. Partly in response to congressional direction, we are working to improve information on the number and costs of contractors employed by DOD.

We are also working to further improve training for financial managers by implementing a course-based certification program similar to the one available to or now in place for acquisition managers.

Financial managers have partnered with the deputy chief management officers to ensure implementation of proposed efficiencies. Last year DOD proposed efficiencies in streamlining totaling \$178 billion in fiscal year 2012 to 2016.

We recently completed an internal review of plans for achieving those efficiencies, and I am pleased to report that the Services and

agencies, I believe, are developing credible plans and processes to meet these demanding goals. They are clearly taking this effort seriously.

We have also made progress improving financial information and achieving audit readiness. That is a topic I know that is of particular interest to this panel. It is of particular interest to me.

We have already achieved and are maintaining auditable statements in some key entities—the Army Corps of Engineers, a number of our defense agencies and several of our large trust funds. But it is also clear that the greatest audit challenges lie ahead, especially the need to move the military services toward auditability.

In addition, there are enterprise-wide weaknesses in DOD financial management which require an enterprise-wide response. To pass an audit, an organization has got to have systems and processes that record financial results of business events in a consistent and reliable manner.

Our processes and systems don't always meet that standard. Many of the systems are old. They don't record information in the level of detail that is required for an audit. Our processes are sometimes variable across commands, even across bases.

These issues are especially challenging in the Department of Defense, because DOD's enormous size and geographical dispersion mean we just can't rely on manual solutions or workarounds, as many other agencies have been able to do.

To deal with these enterprise challenges and to improve financial information and achieve audit readiness, we revised our approach that we have taken—and obviously it hasn't worked—over the past 17 years since the Government Management and Reform Act.

Since August 2009, our emphasis has been on improving the quality of our data and moving toward audit readiness with the information that we use to manage the Department every day—specifically, budgetary information, because we manage the Department based on budgets, and the accounts and location of our assets, which is key to our warfighters. Auditors call it existence and completeness.

We have also put in place a cost-effective approach for dealing with other information required for full auditability. Less than 2 years have passed since we launched this new approach. I can say without hesitation or reservation, financial auditability is now readily acknowledged as a high priority in the Department, and that was not true in some previous terms that I have served in the Department. And we have made noteworthy changes.

We have a clear governance process. There is somebody in charge here. It is the Chief Management Officer, the Deputy Secretary for the Department of Defense, supported on a day-to-day basis by the Chief Financial Officer—me—and also the Deputy Chief Management Officer and an analogous organization at the service level, the CMOs [chief management officers], the under secretaries in that case in charge, aided by their assistant secretaries for financial management and also the deputy chief management officers.

We have established long-term and, more importantly, short-term goals, which are actively managed by our governance process. We need to have goals that we can check are happening over the next couple of years, not just 2017.

We ensured that each military department has programmed adequate resources to support this refocused strategy, and they have done that over the full Future Years Defense Plan [FYDP], so out 5 years.

We now require that senior executive performance appraisals for both financial and nonfinancial personnel include financial audit goals where they are relevant. So we are trying to get this outside the comptroller community.

We are assembling teams within each military department that will be tasked with improving financial controls. I have told you, they are too variable and sometimes they don't meet our audit standards. We have got to fix them. The systems will help, but they alone are not this full solution.

We are in the process of establishing a course-based certification program for defense financial managers that I hope will provide a framework and, among other things, ensure that we provide training to our people on accounting and audit issues.

And we have maintained a close working relationship with our oversight bodies, including the Government Accountability Office and the Department's Inspector General. I have personally briefed Gene Dodaro, the Comptroller General, on this plan, also Gordon Heddell, the DOD IG [Inspector General].

In addition, we have focused on improvements in business systems, and I would like now to ask my colleague, Beth McGrath, to discuss our system efforts.

STATEMENT OF HON. ELIZABETH A. MCGRATH, DEPUTY CHIEF MANAGEMENT OFFICER, U.S. DEPARTMENT OF DEFENSE

Ms. MCGRATH. Good morning. I do appreciate the opportunity to discuss financial management improvements at the Department of Defense.

As the Deputy Chief Management Officer, I am responsible for instituting a framework that clearly defines business goals, develops meaningful performance measures and aligns activities through established and repeatable processes.

The purpose of DOD's overarching management agenda is to establish an effective, agile, innovative business environment that is fiscally responsible.

This business environment includes many IT solutions, which are essential enablers of a broader set of innovative business operations, rather than an end only unto themselves. While I acknowledge past challenges, there are number of things that we are doing, putting together these programs to ensure that they are on the right path.

To ensure that the future programs are structured for success, we are deliberately tying acquisition decisions on our major programs with business outcomes, such as financial auditability.

We are ensuring a program's complete proper business process reengineering to make certain we are not automating inefficient processes and that the Department is prepared for the new system and the process prior to implementation.

By analyzing business investment from a cross-functional perspective, Mr. Hale noted that we are ensuring that the financial

auditability goals are part of other than financial managers' performance appraisals. It is because of their significant contribution to our ability to achieve audit readiness. That takes everyone. Every functional area must participate.

We are adopting a concept of end-to-end processes and standard development methodologies into the business enterprise architecture, together this will enable a more holistic way of thinking into the management of our business operations and ensure we have a shared understanding of our architecture so that we can achieve the interoperability that we are discussing.

We are implementing a new acquisition process for our defense business systems that are tailored to meet the requirements of the business area. Guidance for this process, called the business capabilities life cycle, has been released and is being used today.

Our goal is to deliver a streamlined 21st century systems environment consisting of I.T. capabilities that work together to support efficient, effective business operations.

I would like to note that GAO's removal of the DOD personnel security clearance program from its high-risk list is a significant first in the Department. And it owes its success to our commitment to this results-oriented, end-to-end approach that I just described.

In closing, we are committed to improving management and acquisition of I.T. systems, as it contributes to the overall business operations, again, to include financial auditability. These issues receive significant management attention and are a key part of our overarching strategy to build a better business environment, business processes and systems that create results our men and women in uniform need.

I look forward to continuing our work with this panel as we strive together to a greater efficiency and effectiveness and to create an agile business space enabled by modern, interoperable I.T. solutions. I look forward to your questions.

Secretary HALE. Okay. So we have made a lot of process improvements in business systems, governance, funding. But I want to do more than that. We need to actually start doing some audits and validations. It will focus us on the real problems.

And so we have begun doing that. We have launched an audit of the Marine Corps' statement of budgetary resources. If successful, this would be the first time any military service has actually completed an audit of a financial statement. And we are learning a great deal.

We have brought an independent public accountant in—and they do this for a living, so they know what the problems are. We have learned so much from that audit already.

In May, we began a DOD-wide examination and validation of our funds control and distribution process. It is known in audit terms as appropriations received. Again, an independent public accounting firm is doing that for us. I expect this validation will yield positive results next month.

Periodic validation of our funds control process is very important to me. It also should be important to you, because it will reassure you that we are issuing and controlling our funds in ways that ensure we comply with the laws that you enact.

In June, we began a validation by a public accounting firm of the Army's new General Fund Enterprise Business System, its enterprise research planning system, GFEBS, at those bases where GFEBS has been installed and is mature.

This is also very important, because it will identify areas that must be improved—and there are going to be some, I am sure—to be sure that we are using that system in a manner that is auditable. I am not so worried about the system. I am worried about all the feeders and the processes that are associated with it.

And I don't want to get these systems deployed throughout the Department of Defense and find out, or have somebody find out 3 or 4 years from now, that they are not auditable. So we will cycle through the other Services with that same approach as we can.

In July, we tasked the public accounting firm to validate the Air Force's processes and controls to reconcile their accounts with Treasury, essentially our checkbook with Treasury. It is called funds balance with Treasury. And, again, another key step, and I am cautiously optimistic we will get positive results there.

And by the end of this calendar year, we expect to begin several other validation efforts, including accounts and locations of large portions of our military equipment.

In short, I would tell you there is still a lot to do. I have focused on the positive side, but I am not naive. We have got a long way to go. There are still enterprise-wide weaknesses that we have not resolved. We need to institute a culture of financial controls in the Department, consistent ones that don't yet exist.

But we are committed to improving financial information and audit readiness in the Department of Defense, and I believe we have made significant progress. Our goal is to achieve fully auditable statements by 2017.

That concludes our opening statement, and after Mr. Khan finishes, we welcome your questions.

[The joint prepared statement of Secretary Hale and Ms. McGrath can be found in the Appendix on page 32.]

Mr. CONAWAY. Mr. Khan.

STATEMENT OF ASIF A. KHAN, DIRECTOR, FINANCIAL MANAGEMENT AND ASSURANCE, U.S. GOVERNMENT ACCOUNTABILITY OFFICE

Mr. KHAN. Thank you.

Good morning, Mr. Chairman, Ranking Member Andrews and members of the panel. It is a pleasure to be here today to discuss DOD financial management improvement efforts and how it is going to achieve auditability.

At the outset, I really want to thank this panel for inviting us here. We believe that focused attention, such as these panels, is the key to corrective actions within the Department of Defense.

In my testimony today, I am going to be providing GAO's perspective on the status of DOD's financial management weaknesses and the efforts to resolve them.

In addition to that, I will also touch upon some of the challenges, which DOD continues to face in improving its financial management operations. My testimony is based on our prior work within the Department of Defense.

Regarding the status, for more than a decade, DOD has dominated GAO's list of federal programs and operations at high risk, due to their susceptibility to fraud, waste, abuse and mismanagement.

In the last 20 years, as a result of significant management weaknesses, none of the DOD military departments—Army, Navy or the Air Force—have been able to prepare auditable financial statements.

DOD's past strategies for improving its financial management have generally been ineffective. But recent initiatives and what we have heard this morning are encouraging and show promise.

Specifically, recent changes to the DOD plan for financial improvement and audit readiness, the FIAR plan, if implemented effectively, could result in improved financial management and progress toward auditability. The Army, Navy, Air Force and the Defense Logistics Agency have key roles in implementing the plan.

However, DOD does face many challenges in overcoming its long-standing financial management weaknesses. I am going to briefly highlight six of these major challenges.

The first one, one of the toughest challenges in implementing the FIAR plan is sustaining committed leadership. The DOD comptroller has expressed commitment to the FIAR goals and has established a focused approach to achieving the FIAR long-term goals that is intended to help the DOD achieve near-term successes as well.

To succeed in the long-term efforts to improve, financial management needs to be cross-functional. DOD agencies and offices that perform business functions—for example, weapon system acquisition, and supply chain management—have to work together, as financial management function is dependent on the information received from these two functions and, vice versa, these two functions also need financial management information in order to perform their functions effectively.

However, within every administration and, of course, between administrations there are changes in leadership. It is paramount that the FIAR plan and other current initiatives be institutionalized throughout the Department at all working levels.

The second one is a competent financial management workforce, with the right knowledge and skills, is needed to implement the FIAR plan. Effective financial management requires a knowledgeable, skilled workforce that includes individuals who are trained and well-versed in government accounting practices and information technology.

Analyzing skills needed and then building and retaining an appropriately skilled workforce are needed for DOD to succeed in its transformation effort.

The third one is the accountability and effective oversight of the improvement efforts. DOD has established bodies responsible for governance and oversight of the FIAR plan implementation. It will be critical for senior leadership in each of the DOD components to ensure that oversight of the financial improvement projects and efforts is effective, and that responsible officials are held accountable for the progress.

Fourth, a well-defined enterprise architecture. For DOD, a key element of modern financial management and business operations is the use of integrated information systems with a capability of supporting a vast and complex business operation.

A well-defined enterprise architecture will be needed as DOD blueprints for modernizing its business systems. However, DOD has yet to address previously identified issues associated both with the architecture and investment management.

The fifth one, which is linked to the prior points I have made, is enterprise resource planning, or ERP systems. These are expected to form the core of the business information systems and the DOD components. Their effective implementation is effective to improving DOD financial management and related business operations, and will be key to becoming auditable.

However, the components have largely been unable to implement ERPs that deliver the needed capability on schedule and within budget. Effective business system modernization across DOD is key to achieving hundreds and millions of dollars in annual savings.

Finally, weaknesses in DOD's internal controls over financial management are a pervasive and primary factor in DOD's inability to become auditable. DOD needs a practical approach to prioritize these internal control weaknesses and to correct them within a reasonable period of time.

In closing, I am encouraged by the recent efforts shown and the commitment by DOD leadership, however the Department's ability to address these six weaknesses, or the six major challenges, that I have highlighted today will be a major factor in reaching auditability.

Mr. Chairman, these are my remarks for the morning. I will be happy to answer any questions that you have. Thank you.

[The prepared statement of Mr. Khan can be found in the Appendix on page 43.]

Mr. CONAWAY. All right, Mr. Khan.

Thank you, panelists.

Without objection, I think everybody will go on the 5-minute clock so that we get a lot of the way through. So I will start us.

Bob, yesterday you talked to the Senate about the most recent analysis on the FIAR, that you had made 5 of the 25—

Secretary HALE. You had a spy there, sir.

Mr. CONAWAY. We pay attention, or try to. Five of those short-term goals and you have now extended 20 of those. Were there consequences to the folks who did the 5 versus the folks who did not get the 20? Is your accountability system in place yet to hold managers accountable for that? Has it been implemented?

Secretary HALE. You know I think we are still getting the point there, and certainly nobody was fired and shouldn't have been in that regard. Many of those were interim goals. As I have told you we have met a number of them. We are going to meet within this fiscal year the key goals that concern me—the appropriations received, funds balanced with treasury, the GFEBs, and continue with the Marine Corps audit.

We did miss some of the interim goals and, frankly, it was probably because we didn't plan them well, so I think at this point I

don't feel disciplinary action is appropriate. I think encouragement is what is appropriate. We are making progress.

I was taken aback by the numbers, but I believe she was right, Mr. Chairman. Senator Udall had made that comment yesterday. We did miss a number of the interim goals, but I think we have hit the key goals, at least within the fiscal year.

And we have got to pick up the pace. I understand that. I am hoping for a learning curve here, both in terms of our ability to plan what we can carry out, but also our ability to know how to do it.

Mr. CONAWAY. Let me pivot over to Ms. McGrath, then. The senior executive staff—what is the S for, the SES, Senior Executive—

Ms. MCGRATH. Service.

Mr. CONAWAY [continuing]. Service now has performance measures built into their evaluation process. Have you been at it long enough to have gone through a cycle yet where you put the SES folks through a specific analysis of what their performance goal was versus what they did?

Ms. MCGRATH. Sir, we certainly did that during last performance year's cycle at the, lets say, at the OSD [Office of the Secretary of Defense] level. They were proliferated across the OSD, and they were established for the military departments going into this year's cycle. And we are just at the tail end of this performance year.

Mr. CONAWAY. Can you talk to us about what did and didn't happen to folks who either had a satisfactory performance against the goal they were assigned or did not have satisfactory performance? Any actions taken at this stage?

Ms. MCGRATH. So, certainly, the overall performance. The Department has embedded financial audit goals into its overarching—

Mr. CONAWAY. Right, but try to get down to the individual level, because—

Ms. MCGRATH [continuing]. Performance—

Mr. CONAWAY. Has anybody actually been—yet—held accountable for not getting something done they were supposed to get done?

Ms. MCGRATH. So, I would say yes. The Department's overall performance against all of our goals, it would contribute to their—I will call it their bonus calculation. So those have been in place, and what we have done in the existing year is proliferated them outside the financial space. So the short answer is yes, they have. They have been in place.

Mr. CONAWAY. Given that it is inappropriate to share individual names in here because of the privacy issues, I do think it is going to be helpful to those on the panel to see where—at least some statistics that folks who didn't meet their goals were not as well—they did not get compensated for not making those goals, and folks who did make those goals are, in fact, compensated. So that would be one of the things that we look at.

I want to talk briefly in my time remaining on legacy systems. The folks on this side of the table are trying to figure out ways to kind of watch what goes on. The folks on your side of the table will know abundantly more about what is going on than we will. One

of the measures that I am going to try to focus on and look at is continued legacy systems.

We asked some folks in the Army yesterday once they got the GFEBS done across all 211 sites, having legacy systems would go away. There are about 150-something sites now, so there would be a ways to go. But at some point, we need to do a meaningful job in the number of legacy systems being maintained.

So is that a good tracking metric, Bob, or not?

Secretary HALE. I think it is. I am going to ask Beth to add to that, because it is more in her lane. But I believe it is. You will need to be patient, and GFEBS made a decision not to try to bring all the old data, past data, into the system. That greatly speeds up our ability to deploy this.

It also means that for a period of time we are going to have to operate the old systems so that we can keep track of the legacy data, if you will. So it will be a number of years before they go away.

The other Services have chosen a different approach. That is to bring the old data into the system. That means a huge job of data cleanup, which just slows the implementation.

I am not sure which one is right, you know. I will go with their judgments, but yes we do need to get rid of legacy systems there.

Ms. MCGRATH. But I would add that we currently published an enterprise transition plan that identifies our target solutions like the Army's accounting solutions, GFEBS solution that we have talked about a couple of times.

In the enterprise transition plan, it identifies sunset dates for the legacy systems associated with the implementation of GFEBS. And so we do identify those with dates, and we monitor those as well—again, tied to auditability but also reducing and rationalizing our overall I.T. footprint.

Mr. CONAWAY. Thank you. Rob, for 5 minutes.

Mr. ANDREWS. Well thank you for the testimony. It appears that there has been some substantial progress in the Marine Corps area, Secretary, which you referred to. What are the lessons learned from that? What has led to the relative better progress in that area? I am sure it is a smaller organization. That has a lot to with it. But what has led to the better progress there? And what have we learned that still need to be done there?

Secretary HALE. Well, I think the reason, and you know, frankly, the Department of Navy in general is ahead. All of the other Services are working to catch up. The inter-service rivalry is a very powerful tool in the Department.

Mr. ANDREWS. We have heard this.

Secretary HALE. And I will work this whenever I can. I learned that as the Air Force F.M. [Financial Manager]. And the Navy has been investing steadily over the past 5, 7 years. That is why they are ahead. And the Marine Corps in particular has strong commitments, so—

Mr. ANDREWS. Investing in personnel training, software?

Secretary HALE. Both dollars, I think, and personnel, both—and across the board, not just the Marine Corps, although the Marine Corps is particularly focused. But we have learned a great deal. I mean, we learned, first, that we don't know what we don't know.

We don't really fully understand in the Department of Defense what you have to do to pass an audit for military service, because we have never done it. And you can't learn to swim on the beach. It is hard to talk to other agencies that tend to be different from us, so as the Marine Corps jumped in to try to swim, they found out they had a number of problems.

Some of them were system related, although they have got a pretty decent and fairly integrated system. The real problem is with business processes. We are just doing some things which are effective in terms of meeting war fighter needs, but aren't auditable.

For example, we do bulk obligations of military pay. The auditors want it done in a much more detailed fashion. Sometimes we weren't doing basic and blocking and tackling appropriately.

For example, we weren't taking people off access lists of financial systems when they left the base. They were busy. They didn't get to it. The auditors looked and said, "Hey, there are people here that shouldn't have access." So we have got to correct those kinds of business processes.

Mr. ANDREWS. Does the Department of the Navy have more people relative to the size of the organization working on this problem, or do they have the same number of people doing it more effectively?

Secretary HALE. I think they have in the past. Now I am less sure, because the other Services have definitely bulked up here, and in terms of funding, they are right up. I have kind of used the Navy as a benchmark, as I have looked at the other Services, figuring they are making progress, probably need similar resources. And the other Services are coming up to that level.

Mr. ANDREWS. Mr. Khan, one of the things that you have mentioned in your testimony is major weapons system maintenance and operating and support costs. Do you have any suggestions as to how we might require estimates of those operating support costs be billed into the up front statement of the weapons system?

In other words, one of the problems that has plagued us for a long time is we buy a weapons system and it winds up costing an awful lot more than we thought it was going to—in part, because of the requirement creep, in part because of other problems, but I think also in part, because we understate the operating and support cost.

What suggestions do you have that we might require bidders to build into their costs so that we can more accurately anticipate what is coming?

Mr. KHAN. I mean, certainly this issue starts with process, really, that start in acquisition.

I am sorry, can you hear me now. I am sorry.

It does start in the acquisition process and what Ms. McGrath mentioned that DOD is implementing, an end-to-end process so that when you have a procurement, when you raise a purchase order, you begin to collect all the data which is necessary for accumulating the actual cost which is going to be spent on that particular product itself.

So, I mean, in our work, we have seen that. That is slow to happen in acquisition to link that up with capturing the cost informa-

tion, which can be meaningfully built into, if you will, a profile, whether its weapon systems or even in the large system acquisitions.

I think that will go a long way towards having more of a discipline so that you can true up the estimates with what the actual costs are.

Mr. ANDREWS. Your agency did a compelling study that said we were \$297 billion in cost overruns in seven major weapons systems, I believe it was. Could you just guess what percentage of that \$297 was misunderstanding of support and maintenance costs?

Mr. KHAN. That would be a tough guess. I am sorry.

Mr. ANDREWS. If you would supplement the record later, I would be curious.

Mr. KHAN. Okay.

Secretary HALE. I believe I would let GAO supplement it, though. That was looking at—those were the selected acquisition reports, and they were looking at the procurement on the investment costs associated with the weapons. I don't believe that any of that was associated with that.

Mr. ANDREWS. I think you are right. I think I would modify my question to say, could you make an interesting projection as to what follow-on costs behind the \$297 are going to come because of this problem. That is a better way to frame it. It may be worse, but—

Secretary HALE. May I add a brief point—may I add a brief point to that?

Mr. ANDREWS. Sure.

Secretary HALE. A major issue in the Department has been, as long as I have been associated with DOD, we tend to be overly optimistic about projections of operating and support costs, and we don't make decisions based on them. And you have to make that decision very early in the life of a weapons system to have any meaningful effect.

In some cases we are paying for game-changing capabilities. I think stealth capability has been extremely costly, because every time you exercise with a weapon and it hits a rock or a bird, you have got to recode it. If you have to do maintenance, you have to recode it. It is very expensive.

On the other hand, it has been a war fighter game change. So I wouldn't always say higher operating costs are a bad idea. You have to judge them against what you get.

Mr. CONAWAY. Thanks, Rob.

Scott, for 5 minutes.

Mr. RIGELL. Thank you Mr. Chairman.

I certainly thank our panel for getting up early.

Mr. Chairman, I commend you for starting on time. I think in my 6 months here, this is the first and only meeting that has actually started on time. I am impressed by that.

I also want to thank the Ranking Member Andrews. I think the tone that has been set here is the tone that we need set. I think it is actually, if I can go as far as to say, it is beyond bipartisan. It is just American, you know, us trying to get our hands around this and work together.

And I think that we are here today talking about the challenges faced in the accounting of DOD is of no surprise, given the rapid increase in funding and the mission that was given to DOD after 9/11.

Mr. Hale, I wanted to ask you, given the complexity of DOD, it seems like this of all endeavors we would have to slow down and be very thoughtful and very strategic about how you get your arms around this challenge here.

And have you identified global challenges, those barriers that inhibit our ability to produce audited statements and on a global scale, but identified maybe a smaller sector that we could go after and see if we could get real success in a smaller sector?

I know the government likes to have these acronyms and things like a center of excellence and then ramp it up and move across. Now, I don't know if that is a profound statement at all. You may have done that. Maybe that is reflected in the success that you have had in the Marine Corps. But if you could comment on that, it would be helpful to me.

Secretary HALE. First off, we have been pretty good at slowing down over the years. I am not working to do that. I would like to speed up.

There are two broad problems that we have had in the challenges we face. I would say one is better systems. Especially the Army and Air Force feel that their current systems simply cannot support auditability. Now I will give you just one example to try to make that more concrete.

These systems don't keep track of data at the invoice level. And so when an auditor wants to check our payment, they want to see an invoice. They want to see a contract that backs up that invoice. They want to see a receiving report. Right now what we have to do if we are going to audit that is manually go out and get those documents.

And when you are doing samples of thousands, you can't do it in a timely fashion. The new systems keep track of this data so you literally can hit a button, if it is working right, and you will have the data available. So especially the Army and Air Force feel they must have a new system. So that is one global problem.

The other ones are business processes or financial controls which are too variable and in some cases not strong enough to support audits. I mean, I would say they are reasonable. I know where we are spending the money in budget terms, and I would argue with those who say differently. But they aren't good enough to support audits.

So we are going to have to improve them. We are working on teams to try to identify those and get our commands to start making changes now at the same time they are doing the systems. I don't want to do this—I don't want to do it—I want to do it concurrently, not sequentially.

Finally in terms of your—you have hit exactly what we are trying to do. We are trying to do this in a phased manner. The Marine Corps is a good first step, and these validations are also looking at pieces of this. And so we will learn, and I hope build up some successes, as well as areas where we need to improve.

Mr. RIGELL. I appreciate the answer. Maybe the second part of the question is still a bit unclear to me.

Have we identified a smaller sector, maybe a division, a branch to say this is the one that we are really going to do very, very well, and then we are going to scale this up—lessons learned, best practices. And has that been done? Or is it more you are trying to get your arms around the whole thing?

Secretary HALE. No, I think we have done exactly what you are saying. First, we picked budgetary information as our major focus. And the reason we did that is because it is most used to manage. Then within that, the Marine Corps is our smallest service. It is also the least complex, because the Navy handles a lot of its procurements. And so it is a good starting point, and we are learning a great deal.

But I don't want to just focus on the Marine Corps and have the Air Force—

Mr. RIGELL. That is okay. I think I—

Secretary HALE [continuing]. And the Army sit over there and do nothing.

Mr. RIGELL [continuing]. A lot of Marines on the panel. That is okay.

Secretary HALE. We are counting on the Marine Corps for a financial beachhead and to hold it, too.

I want the other Services to be active. We can't audit their whole statement yet. We are not close enough to do that. So that is why we picked these validations. We are picking pieces that are key—the Air Force for funds balance with Treasury, the Army to look at its systems—

Mr. RIGELL. I am not—

Secretary HALE. We have a phased approach—we call them waves—

Mr. RIGELL. Okay.

Secretary HALE [continuing]. That attempts to do this.

Mr. RIGELL. Thank you.

In my remaining 15 seconds, could you provide the committee—we may have this; I don't believe we do, though—could you provide the committee with the observations and recommendations from the outside auditors? And I am not talking about reams of papers, but if you could condense that, summarize it.

What are the outside auditors, to the extent that that can be summarized in, you know, four or five pages, and specifically if there were any legislative—and this may be going to the end of the book, the last page of the book, but are there any legislative suggestions that they may have made?

Thank you, Mr. Chairman.

Thank you, Mr. Hale.

[The information referred to can be found in the Appendix on page 73.]

Mr. CONAWAY. All right thanks.

Tim, 5 minutes.

Mr. RYAN. Thank you, Mr. Chairman.

I am reading here through the GAO report, and one of the issues that they brought up here is the limited ability to identify, aggre-

gate and use financial management information for managing and controlling operating and support costs.

What are you specifically doing to try to get that more information? And how much of that—I would imagine a good deal of it—you will be interfacing with contractors to try to get that information?

Secretary HALE. Yes. Certainly, in some cases we will use contractor support, although the overall process has to be led by government employees.

First, I would say that for budgetary information, I mean, when you make an appropriation to us, we can track whether or not we meet that appropriation. The appropriations received that I spoke of is the process we use at the start to distribute the money in a manner consistent with the laws the Congress enacts.

And then we do have ability to track that. And I can go through—you heard it when I was giving the briefing a week ago; if you want I will go through it again—but there is some external corroboration of that. We have about 3,000 auditors watching every program and financial move.

Generally, our violations of the Anti-Deficiency Act, which essentially says you weren't doing what the law told you, are quite low—very much lower, I might add, than nondefense agencies taken as a whole. So I have reasonable confidence in the data, that we know where we are spending the data as you tell us.

What gets hard is when you want to start getting cost data, which is very important. When you want to figure out what the JSF, Joint Strike Fighter, costs to operate, that requires special studies. Our systems just can't do that.

We can do the studies, but they take time, and so we need to improve there. And overall, we do need audits to verify that the information is correct. Now, I am pretty sure it is in the right spots and, therefore, I have reasonable confidence in the data we are using to make decisions. But I fully accept that we need audits to verify that point.

Mr. RYAN. So, well, I am not an accountant, so I am trying to—

Secretary HALE. Neither am I.

Mr. RYAN [continuing]. Wrap my brain around this. You are not getting enough good information. Is that fair? Is that what the GAO is saying here?

Secretary HALE. Certainly—

Mr. RYAN. So what are you doing to get more information to eventually figure this out?

Secretary HALE. I would say its in some cases we don't have good information, and overall we don't have audits to verify the quality of that information. There are some good points, like I said. I think our budgetary information—when you appropriate something in Army weapons and track combat vehicles and tell us to spend it a certain way, we can track that.

Mr. RYAN. But what it says here—and maybe GAO would like to chip in here—I mean, what your report here is saying is that this is a repair costs, maintenance, contract services. It seems—feel free to chime in, too—you know, it seems like those are pretty standard requests to know, okay, on the Joint Strike Fighter what are the repair costs? What are the maintenance costs?

And I am having trouble figuring out what the issue is here.

Mr. KHAN. Let me just—oh, I am sorry. Turned that off.

Let me just build on my response to Mr. Andrews' question. The issue is cost here. I mean, DOD does have very good estimates, which they have developed themselves. But they have to be trued up with the actual cost information.

And that is where acquisition process comes into it, because they are the primary people dealing with the contractors. So it has to be set up front the expectation with the contractors that they need specific cost information to be broken down in a certain way, which DOD systems and DOD processes can take into their systems to be able to develop that and match that with the estimates.

Mr. RYAN. Okay. So are we doing that with the contractors now?

Ms. MCGRATH. So part of the today's environment, as Mr. Hale has articulated, the systems weren't designed to do cost accounting. And I am not an accountant either. But as Mr. Hale also articulates, we know where the money goes. It is the actual costs of doing, you know, repairs and those kinds of things.

Mr. RYAN. Right.

Ms. MCGRATH. And so the enterprise resource planning systems, many of those systems that we have been talking about, the target solutions are being designed such that we can capture that cost information, have the actual data that says that we can do forecasting for maintenance and sustainment of those systems, so that we are actually using real data to establish both our inventory needs and our forecasting.

So it is a long way of saying that we are through the development of the business center enterprise architecture. We are developing standard financial information standards along with logistics based standards to ensure at the end of the day that we can aggregate the data, have the cost information so that, you know, that we can have those estimates that GAO has articulated that we don't currently have today.

Mr. RYAN. Okay. I am out of time.

Thank you, Mr. Chairman.

Secretary HALE. If I can take one more shot, because I don't feel I have been helpful.

Let me take the JSF as an example. If you want its operating costs, you are going to have to look at our personnel information, you are going to have to look at our day-to-day operation and maintenance information, you have to look at spare parts.

Those all are in separate appropriations. If you wanted that now, you could not punch a button and get it. You would have to get a team of experienced analysts to go in, look at the budgetary data in those categories, in some cases estimate what portion were attributable to the JSF and come up with that data.

When you are done with that study, I think you would have reasonable information to make a decision, but it is slow, and we don't have an audit that verifies that all of the information is correct.

So it is a nuanced answer. Yes, I can get something that would help the commander make a decision, but it will take a long time, and it will require specialized expertise, contractors and others. And, again, there is no audit to verify its capability.

I hope that is helpful. It is not a black-or-white answer. It is not that we don't have any information. It is just not as readily available, and sometimes it is not as high quality as I would like.

Mr. CONAWAY. It is still a good rationale for continuing pushing on this issue to get this done at the end of the day.

Secretary HALE. Yes, but, you know, to be honest, even if we got an audit, it wouldn't solve—

Mr. CONAWAY. No, no, no, but you can have systems in place, and you would sustain the audits and do those kinds of analysis quicker—

Secretary HALE. You will have—

Mr. CONAWAY [continuing]. More nimble

Secretary HALE [continuing]. Somewhat quicker, yes.

Mr. CONAWAY. And so, Todd Young for 5 minutes.

Mr. YOUNG. Thank you, Mr. Chairman.

Thank you to all our panelists. I do appreciate you being here early this morning.

Mr. Khan, I appreciated your six pillars, if you will, of change that, as you see, must occur in order to really begin to tackle this challenge in a serious way.

I would further reduce those into a few different buckets, if you give me liberty. One would be processes, another would be systems, and then, finally, we have people. And you have put people first in terms of your comments. I don't know if these were order of priority, but it strikes me they were.

Certainly, if we are going to have any sort of lasting change here, we are going to have to have sustaining, committed leadership. We are going to have to institutionalize whatever plans we develop here, and we also need people with the appropriate skill sets to be able to add some value to this overall process.

And so I would ask you or anyone here on the panel, what we have done first to try and—from the beginning, I think we need to be thinking about institutionalizing whatever plans are put in place here. So what have we done to ensure that we are going to have sustaining, committed leadership across administrations, with respect to the FIAR plan?

And then, secondarily, what is being done with respect to assessing the skills needed within DOD in order to make sense of this and to then build that skilled workforce?

Secretary HALE. Perhaps the biggest concern of mine is sustained commitment to this over time. That really depends on—and we have got it right now. I care about this. I learned it in my Air Force F.M. days. I cared about it then. I care about it now.

But, frankly, the people that sit in my chair have generally been—I like to use the phrase “budget junkies.” There is a heavy focus on budget. And I consider myself a budget junkie. I am working constantly, watching what you are doing right now to the budgets. I am very concerned.

So it is important that we have somebody that is my successor or somebody at senior levels who knows something and cares about the audits. I won't be able to do anything about that. I would urge you to do what you can to ensure that. And it will, obviously, be very important that the deputy secretary and the secretary care

about it as well. Sustained leadership over a couple of administrations will be required to make this happen.

Let me turn to the workforce. I think, generally, there are about 68,000 people in the defense financial management workforce, roughly 58,000 government civilians, and about 10,000 of these in the so-called G.S. [grade scale] 500 series, and about 10,000 military personnel. I think, generally, they are well trained. But we haven't been as systematic about that as I would like.

We are starting to do that in two respects: one, completing a competency review—figuring out what they ought to know. I think we generally knew that, but we have to be more specific.

And, second, we have asked for legislative authority, and you have given it to us, as has the Senate, so I hope we will come out of conference, to impose a course-based certification program for defense financial managers, analogous to the Defense Acquisition Workforce Improvement Act legislation for acquisition, which would allow a framework.

And we would require certain courses for certain jobs. And auditability and accounting would be one of them. So I believe that it is, generally, a well-trained workforce, based on my experience with it, especially at the senior levels. But I think a more systematic approach would be appropriate.

You are scowling at me. Did I answer your question?

Mr. YOUNG. Thank you. You did, and, actually when sustained, committed leadership was said, I wasn't necessarily thinking about just the top people in the organization.

And perhaps that is what you meant, Mr. Khan, but I thought institutionally, things might be implemented so that we didn't have a—it didn't require each administration to appoint enlightened people. Maybe we could do things that would ensure that they stayed focused on this problem.

Mr. KHAN. Right, Mr. Young, I mean, that is why I emphasized the human capital of the well-trained workforce. I think that is going to go a long way towards helping institutionalizing some of the topics we are talking about today.

This is to drive transformation. This is change management process. And without having a well-trained workforce in a very complex environment, that is going to be a huge challenge.

I think Congress recognized that. There was a requirement in National Defense Authorization Act of 2006 for DOD to perform a skill set analysis, if you will, and then do a gap analysis of what the to-be requirements are for the skill sets and where they were currently and what the plan was to transition.

So that is going to be key. I mean, it is a complex environment, and then financial management itself is a technically complex area. So you are dealing with several different moving parts here, so the process and systems issue has received attention, but human capital is equally important. And without that the elements aren't going to come together.

Secretary HALE. But I don't think this will succeed unless the secretary, deputy and comptroller and both OSD and the Services care about it and make a high priority of it. It won't happen.

Ms. MCGRATH. Can I also add, though, that we are, from an institutional perspective, baking it into the summary justification of

the budget. So there are performance measures that are identified as part of the budget submission. They are part of the overall GPRA Modernization Act [Government Performance and Results Modernization Act of 2010]. So these are top priorities. It is part of the strategic management plan.

We are utilizing the business enterprise architecture to tie directly to achieving the financial auditability outcome, leveraging the investment review board process, so when systems do come in for development and modernization, there is that connectivity.

And so from an institutional perspective, we are using all of the levers that are there. That notwithstanding, I don't disagree with Mr. Hale's point about the leadership, top-down driven requirement must happen.

Mr. YOUNG. Great. Thank you.

Mr. CONAWAY. Thank you.

To Joe for 5 minutes.

Mr. COURTNEY. Thanks, Mr. Chairman.

Secretary Gates, when he has been before the full committee, has said over and over again that the Department is getting eaten alive by health care costs. Mr. Khan, in your report, you mentioned a problem that GAO identified with TRICARE [DOD health care program] in terms of misclassification.

And I was wondering, first of all, is that just a sort of anecdotal, you know, *sui generis* incident? Or is that something that you think is a broader based problem?

The second question is—and this is just showing my lack of knowledge—is TRICARE done service by service, or is this a program that is administered by the Pentagon in one place?

And given the fact that that is sort of a hot spot in terms of the Pentagon's budget, I mean, is there efforts that are being, you know, focused, in terms of this area, because, again, it is something the Secretary said repeatedly to our committee.

So, Mr. Khan, maybe you can just talk about the report that you submitted.

Mr. KHAN. Yes. I mean, that was an accounting misclassification of information. I mean, that is one instance that we have highlighted. There are several other instances where—I mean, this goes down to the basic fundamentals of bookkeeping, coding of information to make sure that it has correct classification.

These are building blocks of financial reports. If the information is not being accumulated and aggregated at the correct level under the correct classifications, the information is going to be mischaracterized in the financial statements, so you will end up with certain types of information to be understated and other types of information to be overstated.

So this really points towards the importance of having that discipline so that when you pull together the financial statements that you have reasonable assurance that the information that you have in front of you is accurate.

This comes to all the decisionmaking process. If you are making important decisions, if you want to reduce certain activity, where you want to increase activity, or where you can have any cuts, this type of information is going to be very useful.

Secretary HALE. TRICARE is managed centrally in the Department. The Services, obviously, participate, but it is managed centrally.

And, yes, it is a major problem, and we have made two broad proposals: One, to achieve some efficiencies in the TRICARE management agency. And they are working right now to implement those. Can we do it with fewer contractors, fewer people to reduce the overhead?

The other one is to make some changes in the benefits, particularly to working age retirees.

And we have both in the military health care area. We have made a set of proposals, and I very much appreciate the fact that the House supported those proposals in almost all cases. And, generally, the Senate Armed Services Committee has, too, so I would hope that we will get authority, for example, for modest increases in the enrollment fee for working-age retirees in TRICARE and some changes in pharmacy co-pays.

These are tough votes. I recognize that. But some of this is getting out of hand, and we need to begin to make some modest changes in those benefits. So I appreciate your support.

Mr. COURTNEY. Well, again, I understand that certainly one way to save money in the system is to, obviously, shift some costs to the beneficiaries. And, again, that debate has already taken place.

I guess the question is, though, that, you know, what I think we would appreciate is having some confidence in knowing that the program is being administered as efficiently as possible, and the GAO criticism seems to suggest that there are problems there.

And I guess that is sort of, you know, is the Pentagon making efforts to really try and make sure before they come to Congress, asking the beneficiaries to pay more, that, you know, you feel good about whether or not the management is up to speed?

Secretary HALE. We have made a whole series of efforts, prior to proposing those beneficiary increases, to look for ways to hold down the growth in cost.

For example, we were able to use the Veterans pricing scheme for pharmaceuticals, which saved us—I want to say—half a billion a year. I may correct that for the record, but it was substantial savings.

We have looked at a variety of management improvements to deliver the care more carefully. The miscategorization—I need to look more carefully at the GAO report. I don't know enough details to give the answer.

But I can tell you that before we asked for those benefit increases, even though I think they are increases in enrollment fees, even though I think they are fully justified, we tried to do everything we could to try to make the system more efficient.

Can we do more? Yes. There is an ongoing review right now of TRICARE and the rest of the military health system, looking for additional efficiencies. And I would hope that coming out of that would be some further recommendations next year to the Congress.

Mr. CONAWAY. Thanks, Joe.

Rob, you okay?

Mr. ANDREWS. Yes.

Mr. CONAWAY. All right.

Well, then, Bob, Beth, Asif, thank you for coming. I guess, just in concluding here, Bob, and Beth are spectacular professionals. You say all the right things. And to someone who just came walking in and sat down, you would think that you guys almost have it done, because, you know, you are really good at telling us all these things.

As this panel progresses, diving deeper into the weeds, so to speak, I want that sense of urgency somehow to be seen other places, or a sense of urgency seen other places. You know Bob, you told us last week that, you know, nobody gets up thinking about September 30th, 2017, and that you have got to make interim progress, incremental progress to make this happen and a 5 for 25 on that first round on the FIAR plan.

What I don't want to see happen, though, is to set the bar so low on those goes that you go 25/25, because you didn't push yourselves far enough to make that happen. So there is a balance in there. You put it too far out there, and you get discouraged because you don't get there. You put it too low, and you waste time as well.

So this panel is going to be committed to trying to figure out how Congress can put that institutional continuity or sustainability of focus in place so that over these next 6 years that we get this done. You and your predecessors are going to be, you know, integral parts to that. So thank you for coming this morning at 8 o'clock.

Rob, you got any closing remarks?

Mr. ANDREWS. Well, I just want to associate myself with the Chairman's remarks here. We see tangible progress, and we want to work with you to make that happen, but, frankly, the reason this panel exists is to guarantee that progress.

We are hopeful we have a kindred spirit in Secretary Panetta. We know we have kindred spirits on your team, but we want to do more than spirit. We want the body as well. And the panel is on a bipartisan basis committed to that kind of oversight. I appreciate the opportunity to speak this morning.

Mr. CONAWAY. All right.

Thank you all very much.

The hearing is adjourned.

[Whereupon, at 9:03 a.m., the panel was adjourned.]

A P P E N D I X

JULY 28, 2011

PREPARED STATEMENTS SUBMITTED FOR THE RECORD

JULY 28, 2011

**Opening Statement of Congressman Mike Conaway, Chairman
Panel on Defense Financial Management and Accountability Reform
Hearing on
DOD's Plans for Financial Management Improvement and Achieving
Audit Readiness
July 28, 2011**

Welcome everyone to the inaugural hearing for the House Armed Services Committee Panel on Defense Financial Management and Accountability Reform. The Panel met to organize on July 13th and we had our first informal briefing last week. We have adopted an organizational plan, including a detailed work plan, to assist us in examining the progress the Department of Defense has made in improving financial management and achieving audit readiness and identifying the challenges that remain. Without objection, I would like to enter the organizational plan into the record for today's hearing.

But more important than the details of our oversight agenda, Chairman McKeon and Ranking Member Smith have charged this body with making recommendations and providing continuity of leadership on this issue. Therefore, I would like to take a moment to introduce each of the panel members and thank them for their commitment to join Rob and me, as we continue the work of the previous Defense Acquisition Reform Panel.

In addition to my partner, Rob Andrews of New Jersey, the following members will serve on the Panel:

- Scott Rigell of Virginia
- Joe Courtney of Connecticut
- Steven Palazzo of Mississippi
- Tim Ryan of Ohio, and

- Todd Young of Indiana.

The first question on the panel's work plan addresses whether DOD's current financial improvement and audit readiness strategy, methodology, and timelines are appropriate. I feel this is an appropriate starting point as DOD has initiated numerous efforts over the years to address its financial management weaknesses and achieve audit readiness with little or no success. In fact, for over 20 years, GAO and DOD auditors have continued to report significant weaknesses in DOD's ability to provide timely, reliable, and useful information for decision making and reporting.

In these difficult fiscal times, it is absolutely crucial that DOD has reliable information to manage its resources. Having reliable information is especially critical as DOD attempts to implement the \$178 billion in cuts and efficiencies proposed by the former Secretary of Defense, not to mention how important it will be if DOD is forced to look for further significant cuts in the near future. DOD also needs to provide assurance to the American taxpayer that they are not wasting resources. However, because of DOD's poor internal controls, the financial management area has been on GAO's list of high-risk programs that are vulnerable to waste, fraud, and abuse since 1995.

The National Defense Authorization Act (NDAA) of 2010 requires that DOD's financial statements be ready for audit by no later than September 30, 2017. Today we will hear about DOD's strategy and methodology to get DOD to audit readiness by 2017 and the challenges DOD faces in achieving that goal.

As Mr. Khan alludes to in his testimony, DOD is one of the largest and most complex organizations in the world, which contributes to many challenges DOD faces in resolving its long-standing financial management weaknesses. In fiscal

year 2010, DOD reported that it had over \$993 billion in disbursements and \$1.9 trillion in assets. Many organizations, agencies, and field activities must work together in order for DOD to improve its financial management and achieve auditability.

We do not expect to discuss all the challenges DOD is facing in great detail in this hearing. But, it will be a good start to understanding what DOD is up against in its financial improvement efforts. I expect the panel will hold future hearings that cover in much more detail the challenges DOD is facing and their efforts to resolve the issues.

I thank the witnesses in advance for their testimony and agreeing to be with us at such an early hour. Our witnesses today are:

The Honorable Robert F. Hale

Under Secretary of Defense (Comptroller)

The Honorable Elizabeth A. McGrath

Deputy Chief Management Officer

Department of Defense

Mr. Asif A. Khan

Director, Financial Management and Assurance

Government Accountability Office

I now turn to Rob Andrews for any remarks he would like to make.

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Statement of

The Honorable Robert F. Hale
Under Secretary of Defense (Comptroller)

and

The Honorable Elizabeth A. McGrath
Deputy Chief Management Officer
Department of Defense

before the

House Armed Services Committee

Defense Financial Management and
Auditability Reform Panel

July 28, 2011

Embargoed until released
by the House Armed Services Committee

Congressman Conaway, Congressman Andrews, Members of the Panel, thank you for the opportunity to testify today concerning financial management at the Department of Defense (DoD) and our ongoing efforts to achieve audit readiness. We should note that this is an area of interest to our new Secretary of Defense. Secretary Panetta has asked us to join with other Department leaders to review our plans for financial improvement and report back to him with any suggested improvements.

We would like to begin our testimony today by identifying the key goals for defense financial management as well as several issues we are pursuing to better meet those goals. Then we will focus the majority of our testimony on one of these efforts – namely, efforts to improve financial information and achieve auditable financial statements.

Broad Financial Management Goals

To be successful, defense financial managers must achieve three broad goals:

- Acquire the resources necessary to meet national security objectives.
- Ensure the legal, effective, and efficient use of those resources.
- Maintain a capable financial management workforce.

As we pursue these goals, we rely on the support of a dedicated professional work force of more than 60,000 financial management personnel, who provide our warfighters with the resources and financial services they need to meet national security objectives in every area of the world, including Afghanistan and Iraq. We believe that these financial managers, working with other DoD personnel, are generally meeting the financial needs of our warfighters. They are accomplishing this key goal despite some daunting obstacles including financing a shooting war in Afghanistan, completing the military mission in Iraq, supporting operations in Libya, and maintaining a military that can meet future national security requirements. Their task has been made much more difficult by late appropriations, especially the six-month continuing resolution that we experienced in FY 2011.

Defense financial managers also maintain many effective financial processes and reasonable financial controls in many key areas, especially with regard to control of appropriations. As a result, our violations of the key financial laws are quite low, timely and accurate payments are produced in a very high percentage of cases, and interest payments have been dramatically reduced.

There are, however, some significant areas where DoD needs to improve. We need better and more readily available financial information, especially cost data. In specific areas – such as contractor information – we are actively pursuing better information.

Defense financial managers also need to take the lead in pursuing and implementing efficiencies. All DoD personnel are responsible for the efficient use of taxpayer resources. But financial managers can be of particular help in looking for additional efficiencies and in monitoring the implementation of efficiencies that have been proposed. We can also assist in providing the cost information necessary to assess the viability of new efficiencies and monitor those already proposed.

We also need to continue to strengthen the training and experience of the defense financial workforce. We believe that most defense financial managers are well trained. But the community lacks a framework that indicates what training is most important at various points in financial careers. To remedy this shortcoming, we are taking steps to establish a course-based certification program for defense financial managers that will provide a framework. This certification program will also permit us to emphasize education in key areas including auditability. It will be similar to the program for the Defense acquisition workforce. Each job will require specific coursework in pre-requisites. At this time, we have a working group pulling the details together for our certification program. Both the House and Senate Armed Services committee have provided needed legal authority in their authorization bills, and we hope to put the program in place in FY 2012.

Improving Financial Information and Achieving Audit Readiness

Defense financial managers, in concert with other DoD personnel, need to take the lead in improving financial information and achieving audit readiness. There has already been significant progress toward auditable in several entities. For example, the Army Corps of Engineers has fully auditable financial statements and is maintaining them. Several Defense Agencies maintain auditable statements including the Defense Finance and Accounting Service and the Defense Contract Audit Agency. Several large trust funds managed by DoD are also auditable.

At the same time, it is clear that the most daunting challenges remain ahead, particularly the challenge of moving the Military Services toward auditability. Moreover, we know that there are enterprise-wide weaknesses in DoD financial management, and they demand an enterprise-wide business response. The lack of auditable financial statements for DoD as a whole reflects those weaknesses.

The challenge is especially daunting considering DoD's geographical dispersion and enormous size. Every business day, we obligate an average of \$2 billion to \$3 billion and handle hundreds of thousands of payment transactions in thousands of locations worldwide, including war zones. Given our size and mission requirements, we are not able to deploy the vast numbers of accountants that would be required to reconcile our books manually.

To pass an audit, we must have a business environment – including systems and processes – that record the financial results of business events (such as contract signing) in a consistent and reliable manner. Our current business environment does not always meet that standard. Many of our systems are old and handle or exchange information in ways that do not readily support current audit standards. They were designed decades ago to meet budgetary rather than proprietary accounting standards. They tend to be non-standard and sometimes do not include strong financial controls. In these cases, the consistent application of internal controls becomes critical. Many of the legacy systems also do not record data at the transaction level, a capability essential to audit success.

An Enterprise-Wide Response

To address these enterprise-wide issues, we have put in place a strong governance model. As the Department's Chief Management Officer or CMO, the Deputy Secretary is responsible for Department-wide business operations and management issues. He is supported in this by the Deputy Chief Management Officer, or DCMO.

To inject this holistic, integrated way of thinking into the existing fabric of defense management, the DCMO has established a framework for organizing our Business Enterprise Architecture, business processes, and systems environment into essential end-to-end business processes, such as Budget-to-Report, Order-to-Cash, and Procure-to-Pay. This enterprise-wide approach is building the future business processes and systems environment of DoD, with audit readiness and management information in mind.

Improving the Quality of the Information We Use Every Day

To deal with these enterprise challenges -- and to improve financial information and achieve audit readiness -- we revised our approach from those pursued by DoD in the past.

Our strategy revision was shaped by senior leaders in the Comptroller and DCMO organizations and in the Military Departments and Defense Agencies. We also solicited input from the Office of Management and Budget (OMB), the Government Accountability Office (GAO), and Congressional staff.

In August 2009, we issued a memorandum outlining the new approach, which emphasizes improvements in the quality, accuracy, and reliability of the financial and asset information that we use every day to manage the Department. This approach leads to our current concentration on areas that are most important to defense managers while holding down costs in a period of budgetary constraint. Specifically, we are working on two types of information – budgetary information and existence and completeness of assets.

Budgetary information is critical to leadership at all levels, as people make operational and resource allocation decisions. Our new approach on improving budgetary information will lead to audit readiness for our Statements of Budgetary Resources (SBR).

We are also focusing on the accuracy in the numbers and locations of our mission critical assets. The financial audit elements of “existence and completeness” translate directly into knowing “what we have” and “where it is,” so we can use the equipment in combat and ensure that our acquisition organization is buying only what DoD needs.

We have not ignored other efforts necessary to achieve fully auditable statements. This spring we completed a business case analysis that was required by key stakeholders and included as a provision in the FY 2011 National Defense Authorization Act (NDAA). This analysis provides a roadmap to a cost-effective way for achieving auditability for financial statements beyond the SBR.

The FY 2010 NDAA and subsequent acts accommodated our new approach to financial improvement and audit readiness. We appreciate the support of the Congress and remain committed to have fully auditable statements by 2017.

System Improvements Are Critical to Success

To achieve and sustain auditable financial statements, even using this new approach, we must improve our financial systems.

To accomplish this, we must orient the DoD around end-to-end business processes that support audit goals, implement Enterprise Resource Planning (ERP) systems, leverage those investments to the maximum extent practicable, modernize legacy systems when necessary and supported by a business case, and also aggressively sunset legacy systems that are obsolete, redundant, or not aligned with our business objectives. Our goal is to deliver a streamlined, 21st-century systems environment comprised of IT capabilities that work seamlessly together to support effective and efficient business processes and operations. The DCMO and the Military Department CMOs play an integral role in the governance processes overseeing the implementation of these systems and the processes they enable.

We are focusing on three key areas:

First, we have taken steps to improve our current approach to acquiring and implementing IT systems, particularly in the business domain. Important revisions to the Department's standard acquisition process will be included in an update to the DoD Instruction 5000.2, "Operation of the Defense Acquisition System," for IT systems. These revisions will include an improved acquisition model for our defense business systems, called the Business Capability Lifecycle, which is in use today for a growing number of programs and is an essential pilot effort for our broader IT reform effort. The Deputy Secretary has made clear that one of his highest management priorities is improving the acquisition, development, and fielding of IT systems.

Further, in addition to improving acquisition policy, the Department is working to improve specific acquisition outcomes of its business Major Automated Information System (MAIS) programs through more rigorous acquisition oversight and investment review. The Department is more closely tying business outcomes to acquisition milestones and specifically requiring that individual programs, such as Army's General Fund Enterprise Business System (GFEBs) and Navy ERP, define the role that they play in their organizations' auditability efforts and end-to-end processes. For example, in the last GFEBs Acquisition Decision Memorandum, signed June 24, 2011, we explicitly required that GFEBs:

- Obtain the Under Secretary of Defense (Comptroller) (USD(C)) and Department of Defense (DoD) Deputy Chief Management Officer (DCMO) approval of the end-to-end process and system portions of the Army plan to achieve audit readiness by September 2017 as defined in Financial Improvement and Audit Readiness Guidance. Specifically, the Army plan must address the GFEBs role in achieving audit readiness in the work products defined in phases 1 and 3 of the FIAR Guidance Methodology.
- Obtain USD(C) concurrence that the end-to-end business systems and processes within Army control support auditable financial statements where GFEBs has been implemented and integrated. The USD(C) will rely on the opinion of an independent public accounting firm expressed in an examination of the Army audit readiness assertion of a GFEBs entity currently planned for December 31, 2012 and will allow for remaining minor system and process enhancements scheduled for completion within 12 months.

Second, we are defining a target systems architecture that is modeled on the premise of end-to-end business processes and uses the capability inherent in our ERP systems to the maximum extent practicable. This will minimize the number of required data exchanges and

system-to-system interfaces, thus reducing the potential for error. It will also increase the degree of process standardization and cut down on unnecessary software development.

Third, we will continue to guide our system investments using the Business Enterprise Architecture (BEA), which defines the necessary data standards, business rules, performance metrics, and standard system configurations that will allow our systems to be interoperable. This, along with our Enterprise Transition Plan, will ensure that when data is exchanged between systems, it happens securely and maintains the integrity of the data.

Improved systems alone, however, will not eliminate our weaknesses or guarantee auditable statements. Achieving auditability requires that we apply a consistent level of process controls that cross organizations and functional areas. Business and financial information that is passed from system to system must also be subject to a control environment to ensure that only authorized personnel are using the system and that these systems protect the data quality and maintain a compliant audit trail within the end-to-end business process. This process must be controlled at the transaction level, from the source to the general ledger postings, accurate trial balances, and reliable period closeouts. Only by completing these steps can we prepare financial statements that an auditor can cost-effectively review and verify. Many elements of our current business environment must be changed to allow us to meet financial audit standards. In the midst of two wars and numerous military operations, implementation of our new approach will continue to be a major challenge.

Where We Are Today

Less than two years have passed since we took stock of our previous efforts and decided on new priorities designed to bring the various functional communities together to work toward the common goal of financial auditability. Financial auditability is now accepted as a high priority for the Department. To move forward with our new, focused approach, we have made many changes:

- We established a clear governance process with the Department's Chief Management Officer in the lead and the Under Secretary of Defense (Comptroller) and Deputy Chief Management Officer playing key roles.
- We established clear but flexible guidance, so the components can prepare to assert audit readiness by developing detailed plans for their discovery and remediation efforts.

- We have engaged the Department's CMO (the Deputy Secretary), as well as the Military Department CMOs (Under Secretaries) and the Service Vice Chiefs, in a personal commitment to support our goals.
- We have ensured that each Military Department has programmed adequate resources to move forward with this strategy.
- We established a clear and meaningful linkage between major business system investments and the goals of financial auditability.
- We are requiring Senior Executive performance appraisals to include financial audit goals among their criteria, including functional business areas that generate business events with financial impact. This key initiative will help establish audit requirements in business areas outside comptroller.
- We also are assembling teams within each Military Department that will be tasked with improving financial controls.
- We have maintained a close working relationship with key stakeholders and oversight bodies, including GAO and the Department's Inspector General.

While we have made or are making many process changes, we also recognize that we must demonstrate specific progress to reassure ourselves, and the Congress, that we are actually moving toward auditable financial statements. To that end, we launched an audit of the Marine Corps' Statement of Budgetary Resources (SBR). If successful, this would be the first time that any Military Service has completed an audit of a financial statement. We have already learned a great deal from this effort, and we believe that it will lead to a positive audit opinion.

We are also undertaking a number of other efforts to validate and demonstrate progress. In May of this year we began a DoD-wide examination and validation of our funds control and distribution process (known in audit terms as "appropriations received") by a public accounting firm. Periodic validation of appropriations received will demonstrate to Congress that we are controlling our funds carefully and in ways that ensure we comply with the laws you enact. In June we began a public accounting firm validation of the Army's organizations and bases that have implemented the General Fund Enterprise Business System (GFEBS) business environment, a key effort to ensure that this new system is being used in a manner that is auditable. In July we began a public accounting firm validation of the Air Force's processes and controls to reconcile their accounts with Treasury. This "checkbook reconciliation" is a key building block to auditable financial statements. By the end of this calendar year we expect to

begin several other validation efforts including validations of the counts and locations of large portions of our military equipment.

Conclusion

In sum, we recognize the challenges associated with improving financial management in DoD and especially the challenges related to improving information and achieving audit readiness. To meet audit challenges, we have developed a workable and promising partnership between the CFO and DCMO communities that will help with implementation. We have also implemented a new, focused approach that includes near-term goals, in addition to the long-term goal of achieving auditable statements by the Congressional deadline of 2017.

As we mentioned at the outset of this statement, we are also currently reviewing plans for financial management improvement at the request of Secretary Panetta. We will report back to him and solicit his guidance about future initiatives.

We would conclude by emphasizing that we are personally committed to improving defense financial management as part of our overall commitment to providing the financial resources and business operations necessary to meet our national security objectives.



Robert F. Hale

**Under Secretary of Defense (Comptroller) and Chief
Financial Officer**



As Under Secretary of Defense (Comptroller), Robert F. Hale is the principal advisor to Secretary of Defense Robert M. Gates on all budgetary and fiscal matters, including the development and execution of the Defense Department's annual budget of more than \$600 billion. As Chief Financial Officer, Mr. Hale also oversees the Department's financial policy, financial management systems, and business modernization efforts.

At the time of his nomination by President Barack Obama in January 2009, Robert Hale was Executive Director of the American Society of Military Comptrollers (ASMC), the professional association of Defense financial managers. For three-and-a-half years, he led the society's certification program (the Certified Defense Financial Manager program), as well as training programs, a professional journal, and other activities, including ASMC's National Professional Development Institute, an annual conference which attracts more than 3,500 participants.



From 1994 to 2001, Mr. Hale served in the Pentagon as the Assistant Secretary of the Air Force (Financial Management and Comptroller), where he was responsible for annual budgets of more than \$70 billion, efforts to streamline Air Force financial management, and compliance with the Chief Financial Officers Act.

For the 12 years prior to his Air Force service, Mr. Hale headed the National Security Division at the Congressional Budget Office (CBO), developing quantitative analyses of major defense budget issues and testifying frequently before Congressional committees.

Earlier in his career, Mr. Hale was a senior fellow and head of the acquisition and grants management group at LMI, a consulting firm specializing in service to the Federal government. He also spent three years as an active duty officer in the U.S. Navy and served as a staff analyst and study director at the Center for Naval Analyses.

Mr. Hale graduated with honors from Stanford University with a B.S. in mathematics and statistics. He also holds a Master's degree in operations research from Stanford and an MBA from the George Washington University. He is a Certified Defense Financial Manager (CDFM), a fellow of the National Academy of Public Administration, and a past member of the Defense Business Board.



Elizabeth A. McGrath

Deputy Chief Management Officer for Department of Defense



Ms. Elizabeth (Beth) A. McGrath was sworn in as the Department's first Deputy Chief Management Officer, a Senate-confirmed and politically appointed position, on July 1, 2010. Ms. McGrath leads the Department's efforts to better synchronize, integrate and coordinate DoD business operations and serves as the Principal Staff Assistant (PSA) and advisor to the Secretary and Deputy Secretary of Defense for matters relating to management and improvement of business operations. Ms. McGrath is focused on achieving sustainable and enduring improvements and efficiency and effectiveness in the Department's business related enterprise policies, processes and systems. She also serves as the DoD Performance Improvement Officer and is responsible for formulating the legislatively mandated Departmental Strategic Management Plan.



Ms. McGrath serves as the Milestone Decision Authority for numerous business-focused Major Automated Information Systems (MAIS) and also executes the Department's primary governance body for business transformation, the Defense Business System Management Committee; establishes performance goals and measurements for the Department's business operations; implements the Department's Continuous Process Improvement efforts; and is the Vice-Chair of the Performance Accountability Council that is responsible to the President to reform the government-wide security clearance process. Her responsibilities require extensive integration and coordination across the Department as well as with many Federal agencies, such as the Office of Management and Budget, Director for National Intelligence and the Department of Veterans Affairs.

Previously, Ms. McGrath served as the Deputy Director for Systems Integration, Defense Finance and Accounting Service (DFAS) where she created a financial migration strategy that was executed with a collective budget of approximately \$1B. She managed the entire financial architecture supporting DoD-wide standard financial systems, integrating it with the Department's evolving target, enterprise architecture. Project scope included logistics, personnel, medical, acquisition and financial missions including many information technology solutions.

Prior to joining DFAS, Ms. McGrath served in a variety of program management roles culminating in Program Executive Office-level oversight responsibility. She possesses extensive knowledge of acquisition-related statutes, regulations and policies with over 20 years applied acquisition experience with Major Defense Acquisition Programs and MAIS. She served as the Business and Acquisition Manager on an international torpedo defense program with the United Kingdom and held numerous other financial, acquisition and program management positions within the Department of the Navy.

Ms. McGrath was awarded the Meritorious Executive Presidential Rank Award for Fiscal Year 2008 and the Office of the Secretary of Defense Exceptional Civilian Service Award in October 2008. She holds a bachelor's degree in Economics from George Mason University, is a graduate of the Federal Executive Institute, is certified Acquisition Level III in Program Management, Financial Management and Logistics and is a member of the DoD Acquisition Professional Community.

United States Government Accountability Office

GAO

Testimony
Before the Panel on DOD Financial
Management, Committee on Armed Services,
U.S. House of Representatives

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DOD FINANCIAL MANAGEMENT

Numerous Challenges Must Be Addressed to Achieve Auditability

Statement of Asif A. Khan, Director
Financial Management and Assurance



GAO
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Highlights

Highlights of GAO-11-864T, a testimony before the Panel on DOD Financial Management, Committee on Armed Services, U.S. House of Representatives

Why GAO Did This Study

As one of the largest and most complex organizations in the world, the Department of Defense (DOD) faces many challenges in resolving serious problems in its financial management and related business operations and systems. DOD is required by various statutes to (1) improve its financial management processes, controls, and systems 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 (2) produce audited financial statements.

Over the years, DOD has initiated numerous efforts to improve the department's financial management operations and achieve an unqualified (clean) opinion on the reliability of its reported financial information. These efforts have fallen short of sustained improvement in financial management or financial statement auditability.

The Panel requested that GAO provide its perspective on the status of DOD's financial management weaknesses and its efforts to resolve them, the challenges DOD continues to face in improving its financial management and operations, and the status of its efforts to implement automated business systems as a critical element of DOD's Financial Improvement and Audit Readiness strategy.

View GAO-11-864T or key components. For more information, contact Asif A. Khan at (202) 512-9095 or khana@gao.gov.

July 28, 2011

DOD FINANCIAL MANAGEMENT**Numerous Challenges Must Be Addressed to Achieve Auditability****What GAO Found**

DOD financial management has been on GAO's high-risk list since 1995 and, despite several reform initiatives, remains on the list today. Pervasive deficiencies in financial management processes, systems, and controls, and the resulting lack of data reliability, continue to impair management's ability to assess the resources needed for DOD operations; track and control costs; ensure basic accountability; anticipate future costs; measure performance; maintain funds control; and reduce the risk of loss from fraud, waste, and abuse. DOD spends billions of dollars each year to maintain key business operations intended to support the warfighter, including systems and processes related to the management of contracts, finances, supply chain, support infrastructure, and weapon systems acquisition. These operations are directly impacted by the problems in financial management. In addition, the long-standing financial management weaknesses have precluded DOD from being able to undergo the scrutiny of a financial statement audit.

DOD's past strategies for improving financial management were ineffective, but recent initiatives are encouraging. In 2005, DOD issued its Financial Improvement and Audit Readiness (FIAR) Plan for improving financial management and reporting. In 2009, the DOD Comptroller directed that FIAR efforts focus on financial information in two priority areas: budget and mission-critical assets. The FIAR Plan also has a new phased approach that comprises five waves of concerted improvement activities. The first three waves focus on the two priority areas, and the last two on working toward full auditability. The plan is being implemented largely through the Army, Navy, and Air Force military departments and the Defense Logistics Agency, lending increased importance to the committed leadership in these components.

Improving the department's financial management operations and thereby providing DOD management and Congress more accurate and reliable information on the results of its business operations will not be an easy task. It is critical that current initiatives related to improving the efficiency and effectiveness of financial management that have the support of the DOD's Deputy Chief Management Officer and Comptroller continue with sustained leadership and monitoring.

Absent continued momentum and necessary future investments, current initiatives may falter. Below are some of the key challenges that DOD must address for its financial management to improve to the point where DOD is able to produce auditable financial statements:

- committed and sustained leadership,
- effective plan to correct internal control weaknesses,
- competent financial management workforce,
- accountability and effective oversight,
- well-defined enterprise architecture, and
- successful implementation of the enterprise resource planning systems.

Mr. Chairman and Members of the Panel:

It is a pleasure to be here today to discuss the status of the Department of Defense's (DOD) efforts to improve its financial management operations and achieve audit readiness. At the outset, I would like to thank the Panel for holding this hearing and to acknowledge the important role of such hearings in the oversight of DOD's financial management efforts.

DOD is one of the largest and most complex organizations in the world. For fiscal year 2012, the budget requested for the department was approximately \$671 billion—\$553 billion in discretionary budget authority and \$118 billion to support overseas contingency operations. The fiscal year 2012 budget request also noted that DOD employed over 3 million military and civilian personnel—including active and reserve service members. DOD operations span a wide range of defense organizations, including the military departments and their respective major commands and functional activities, large defense agencies and field activities, and various combatant and joint operational commands that are responsible for military operations for specific geographic regions or theaters of operation. To execute its operations, the department performs interrelated and interdependent business functions, including financial management, logistics management, health care management, and procurement. To support its business functions, DOD has reported that it relies on over 2,200 business systems,¹ including accounting, acquisition, logistics, and personnel systems.

The department's sheer size and complexity contribute to the many challenges DOD faces in resolving its pervasive, complex, and long-standing financial management and related business operations and systems problems. Numerous initiatives and efforts have been undertaken by DOD and its components to improve the department's financial management operations and to arrive at a point where the reliability of its financial statements and related financial management information would be sufficient to pass an audit with favorable (clean)

¹DOD excludes from its business systems those designated as national security systems under section 2222(j) of Title 10, United States Code. National security systems are intelligence systems, cryptologic activities related to national security, military command and control systems, and equipment that is an integral part of a weapon or weapons system or is critical to the direct fulfillment of military or intelligence missions.

audit opinions. To date, DOD has not achieved effective financial management capabilities or financial statement auditability.²

Today, I will discuss the status of DOD's financial management weaknesses, its efforts to resolve those weaknesses, and the challenges DOD continues to face in its efforts to improve its financial management operations. In addition, I will outline the status of the department's efforts to implement its enterprise resource planning (ERP) systems,³ which represent a critical element of the department's Financial Improvement and Audit Readiness (FIAR) strategy. My statement today is based on our prior work related to the department's FIAR Plan⁴ and ERP implementation efforts.⁵ Our work was conducted in accordance with generally accepted government auditing standards and our previously published reports contain additional details on the scope and methodology for those reviews. 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 the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

²DOD's auditors have reported material financial management weaknesses in the following areas: (1) Financial Management Systems, (2) Fund Balance with Treasury, (3) Accounts Receivable, (4) Inventory, (5) Operating Materials and Supplies, (6) General Property, Plant, and Equipment, (7) Government-Furnished Material and Contractor-Acquired Material, (8) Accounts Payable, (9) Environmental Liabilities, (10) Statement of Net Cost, (11) Intragovernmental Eliminations, (12) Other Accounting Entries, and (13) Reconciliation of Net Cost of Operations to Budget.

³An ERP system uses commercial off-the-shelf (COTS) software consisting of multiple, integrated functional modules that perform a variety of business related tasks such as general ledger accounting, payroll, and supply chain management.

⁴GAO, *Financial Management: Achieving Financial Statement Auditability in the Department of Defense*, GAO-09-373 (Washington, D.C.: May 6, 2009).

⁵GAO, *DOD Business Transformation: Improved Management and Oversight of Business Modernization Efforts Needed*, GAO-11-53 (Washington, D.C.: Oct. 7, 2010); *Defense Logistics: Actions Needed to Improve Implementation of the Army Logistics Modernization Program*, GAO-10-481 (Washington, D.C.: Apr. 30, 2010); *DOD Business Transformation: Air Force's Current Approach Increases Risk That Asset Visibility Goals and Transformation Priorities Will Not Be Achieved*, GAO-08-866 (Washington, D.C.: Aug. 8, 2008); *DOD Business Systems Modernization: Important Management Controls Being Implemented on Major Navy Program, but Improvements Needed in Key Areas*, GAO-08-896 (Washington, D.C.: Sept. 8, 2008); and *DOD Business Transformation: Lack of an Integrated Strategy Puts the Army's Asset Visibility System Investments at Risk*, GAO-07-860 (Washington, D.C.: July 27, 2007).

Background

The department is facing near-and long-term internal fiscal pressures as it attempts to balance competing demands to support ongoing operations, rebuild readiness following extended military operations, and manage increasing personnel and health care costs as well as significant cost growth in its weapon systems programs. For more than a decade, DOD has dominated GAO's list of federal programs and operations at high risk of being vulnerable to fraud, waste, abuse.⁶ In fact, all of the DOD programs on GAO's High-Risk List relate to business operations, including systems and processes related to management of contracts, finances, supply chain, and support infrastructure,⁷ as well as weapon systems acquisition. Long-standing and pervasive weaknesses in DOD's financial management and related business processes and systems have (1) resulted in a lack of reliable information needed to make sound decisions and report on the financial status and cost of DOD activities to Congress and DOD decision makers; (2) adversely impacted its operational efficiency and mission performance in areas of major weapons system support and logistics; and (3) left the department vulnerable to fraud, waste, and abuse.

Because of the complexity and long-term nature of DOD's transformation efforts, GAO has reported the need for a chief management officer (CMO) position and a comprehensive, enterprisewide business transformation plan. In May 2007, DOD designated the Deputy Secretary of Defense as the CMO. In addition, the National Defense Authorization Acts for Fiscal Years 2008 and 2009 contained provisions that codified the CMO and Deputy CMO (DCMO) positions, required DOD to develop a strategic management plan, and required the Secretaries of the military

⁶DOD bears responsibility, in whole or in part, for 14 of the 30 federal programs or activities that GAO has identified as being at high risk of waste, fraud, abuse, and mismanagement. The seven specific DOD high-risk areas are (1) approach to business transformation, (2) business systems modernization, (3) contract management, (4) financial management, (5) supply chain management, (6) support infrastructure management, and (7) weapon systems acquisition. The seven governmentwide high-risk areas that include DOD are: (1) disability programs, (2) interagency contracting, (3) information systems and critical infrastructure, (4) information sharing for homeland security, (5) human capital, (6) real property, and (7) ensuring the effective protection of technologies critical to U.S. national security interests.

⁷Support infrastructure includes categories such as installations, central logistics, the defense health program, and central training.

departments to designate their Undersecretaries as CMOs and to develop business transformation plans.

Overview of DOD's
Accounting and Finance
Activities

DOD financial managers are responsible for the functions of budgeting, financing, accounting for transactions and events, and reporting of financial and budgetary information. To maintain accountability over the use of public funds, DOD must carry out financial management functions such as recording, tracking, and reporting its budgeted spending, actual spending, and the value of its assets and liabilities. DOD relies on a complex network of organizations and personnel to execute these functions. Also, its financial managers must work closely with other departmental personnel to ensure that transactions and events with financial consequences, such as awarding and administering contracts, managing military and civilian personnel, and authorizing employee travel, are properly monitored, controlled, and reported, in part, to ensure that DOD does not violate spending limitations established in legislation or other legal provisions regarding the use of funds.

Before fiscal year 1991, the military services and defense agencies independently managed their finance and accounting operations. According to DOD, these decentralized operations were highly inefficient and failed to produce reliable information. On November 26, 1990, DOD created the Defense Finance and Accounting Service (DFAS) as its accounting agency to consolidate, standardize, and integrate finance and accounting requirements, functions, procedures, operations, and systems. The military services and defense agencies pay for finance and accounting services provided by DFAS using their operations and maintenance appropriations. The military services continue to perform certain finance and accounting activities at each military installation. These activities vary by military service depending on what the services wanted to maintain in-house and the number of personnel they were willing to transfer to DFAS. As DOD's accounting agency, DFAS records these transactions in the accounting records, prepares thousands of reports used by managers throughout DOD and by the Congress, and prepares DOD-wide and service-specific financial statements. The military services play a vital role in that they authorize the expenditure of funds and are the source of most of the financial information that allows DFAS to make payroll and contractor payments. The military services also have responsibility for most of DOD assets and the related

information needed by DFAS to prepare annual financial statements required under the Chief Financial Officers Act.⁸

DOD accounting personnel are responsible for accounting for funds received through congressional appropriations, the sale of goods and services by working capital fund businesses, revenue generated through nonappropriated fund activities, and the sales of military systems and equipment to foreign governments or international organizations. DOD's finance activities generally involve paying the salaries of its employees, paying retirees and annuitants, reimbursing its employees for travel-related expenses, paying contractors and vendors for goods and services, and collecting debts owed to DOD. DOD defines its accounting activities to include accumulating and recording operating and capital expenses as well as appropriations, revenues, and other receipts. According to DOD's fiscal year 2012 budget request, in fiscal year 2010 DFAS

- processed approximately 198 million payment-related transactions and disbursed over \$578 billion;
- accounted for 1,129 active DOD appropriation accounts; and
- processed more than 11 million commercial invoices.

Pervasive Financial Management Problems Continue to Affect the Efficiency and Effectiveness of DOD Operations

DOD financial management was designated as a high-risk area by GAO in 1995. Pervasive deficiencies in financial management processes, systems, and controls, and the resulting lack of data reliability, continue to impair management's ability to assess the resources needed for DOD operations; track and control costs; ensure basic accountability; anticipate future costs; measure performance; maintain funds control; and reduce the risk of loss from fraud, waste, and abuse.

Other business operations, including the high-risk areas of contract management, supply chain management, support infrastructure management, and weapon systems acquisition are directly impacted by the problems in financial management. We have reported that continuing weaknesses in these business operations result in billions of dollars of wasted resources, reduced efficiency, ineffective performance, and

⁸ See 31 U.S.C. § 3515(a), (c); OMB Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, Appendix B (Sept. 4, 2007).

inadequate accountability. Examples of the pervasive weaknesses in the department's business operations are highlighted below.

- DOD invests billions of dollars to acquire weapon systems, but it lacks the financial management processes and capabilities it needs to track and report on the cost of weapon systems in a reliable manner. We reported on this issue over 20 years ago,⁹ but the problems continue to persist. In July 2010, we reported¹⁰ that although DOD and the military departments have efforts underway to begin addressing these financial management weaknesses, problems continue to exist and remediation and improvement efforts would require the support of other business areas beyond the financial community before they could be fully addressed.
- DOD also requests billions of dollars each year to maintain its weapon systems, but it has limited ability to identify, aggregate, and use financial management information for managing and controlling operating and support costs. Operating and support costs can account for a significant portion of a weapon system's total life-cycle costs, including costs for repair parts, maintenance, and contract services. In July 2010, we reported¹¹ that the department lacked key information needed to manage and reduce operating and support costs for most of the weapon systems we reviewed¹²—including cost estimates and historical data on actual operating and support costs. For acquiring and maintaining weapon systems, the lack of complete and reliable financial information hampers DOD officials in analyzing the rate of cost growth, identifying cost drivers, and developing plans for managing and controlling these costs. Without timely, reliable, and useful financial information on cost, DOD management lacks information needed to accurately report on acquisition costs, allocate resources to programs, or evaluate program performance.

⁹GAO, *Financial Audit: Air Force Does Not Effectively Account for Billions of Dollars of Resources*, GAO/AFMD 90-23 (Washington, D.C.: Feb. 23, 1990).

¹⁰GAO, *Department of Defense: Additional Actions Needed to Improve Financial Management of Military Equipment*, GAO-10-695 (Washington, D.C.: July 26, 2010).

¹¹GAO, *Defense Management: DOD Needs Better Information and Guidance to More Effectively Manage and Reduce Operating and Support Costs of Major Weapon Systems*, GAO-10-717 (Washington, D.C.: July 20, 2010).

¹²GAO reviewed the following seven major aviation systems: the Navy's F/A-18E/F; the Air Force's F-22A, B-1B, and F-15E; and the Army's AH-64D, CH-47D, and UH-60L.

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- In June 2010, we reported¹³ that the Army Budget Office lacked an adequate funds control process to provide it with ongoing assurance that obligations and expenditures do not exceed funds available in the Military Personnel–Army (MPA) appropriation. We found that an obligation of \$200 million in excess of available funds in the Army's military personnel account violated the Antideficiency Act. The overobligation likely stemmed, in part, from lack of communication between Army Budget and program managers so that Army Budget's accounting records reflected estimates instead of actual amounts until it was too late to control the incurrence of excessive obligations in violation of the act. Thus, at any given time in the fiscal year, Army Budget did not know the actual obligation and expenditure levels of the account. Army Budget explained that it relies on estimated obligations—despite the availability of actual data from program managers—because of inadequate financial management systems. The lack of adequate process and system controls to maintain effective funds control impacted the Army's ability to prevent, identify, correct, and report potential violations of the Antideficiency Act.
 - In our February 2011 report¹⁴ on the Defense Centers of Excellence (DCOE), we found that DOD's TRICARE Management Activity (TMA) had misclassified \$102.7 million of the nearly \$112 million in DCOE advisory and assistance contract obligations. The proper classification and recording of costs are basic financial management functions that are also key in analyzing areas for potential future savings.

Without adequate financial management processes, systems, and controls, DOD components are at risk of reporting inaccurate, inconsistent, and unreliable data for financial reporting and management decision making and potentially exceeding authorized spending limits. The lack of effective internal controls hinders management's ability to have reasonable assurance that their allocated resources are used effectively, properly, and in compliance with budget and appropriations law.

¹³GAO, *Department of the Army—The Fiscal Year 2008 Military Personnel, Army Appropriation and the Antideficiency Act*, B-318724 (Washington, D.C.: June 22, 2010).

¹⁴GAO, *Defense Health: Management Weaknesses at Defense Centers of Excellence for Psychological Health and Traumatic Brain Injury Require Attention*, GAO-11-219 (Washington, D.C.: Feb. 28, 2011).

**DOD's Past Strategies
for Improving Financial
Management Were
Ineffective but Recent
Initiatives Are
Encouraging**

Over the years, DOD has initiated several broad-based reform efforts to address its long-standing financial management weaknesses. However, as we have reported, those efforts did not achieve their intended purpose of improving the department's financial management operations. In 2005, the DOD Comptroller established the DOD FIAR Directorate to develop, manage, and implement a strategic approach for addressing the department's financial management weaknesses for achieving auditability, and for integrating these efforts with other improvement activities, such as the department's business system modernization efforts. In May 2009,¹⁵ we identified several concerns with the adequacy of the FIAR Plan as a strategic and management tool to resolve DOD's financial management difficulties and thereby position the department to be able to produce auditable financial statements.

Overall, since the issuance of the first FIAR Plan in December 2005, improvement efforts have not resulted in the fundamental transformation of operations necessary to resolve the department's long-standing financial management deficiencies. However, DOD has made significant improvements to the FIAR Plan that, if implemented effectively, could result in significant improvement in DOD's financial management and progress toward auditability, but progress in taking corrective actions and resolving deficiencies remains slow. While none of the military services has obtained an unqualified (clean) audit opinion, some DOD organizations, such as the Army Corps of Engineers, DFAS, the Defense Contract Audit Agency, and the DOD Inspector General, have achieved this goal. Moreover, some DOD components that have not yet received clean audit opinions are beginning to reap the benefits of strengthened controls and processes gained through ongoing efforts to improve their financial management operations and reporting capabilities. Lessons learned from the Marine Corps' Statement of Budgetary Resources audit can provide a roadmap to help other components better stage their audit readiness efforts by strengthening their financial management processes to increase data reliability as they develop action plans to become audit ready.

In August 2009, the DOD Comptroller sought to further focus efforts of the department and components, in order to achieve certain short- and long-

¹⁵GAO, *Financial Management: Achieving Financial Statement Auditability in the Department of Defense*, GAO-09-373 (Washington, D.C.: May 6, 2009).

term results, by giving priority to improving processes and controls that support the financial information most often used to manage the department. Accordingly, DOD revised its FIAR strategy and methodology to focus on the DOD Comptroller's two priorities—budgetary information and asset accountability. The first priority is to strengthen processes, controls, and systems that produce DOD's budgetary information and the department's Statements of Budgetary Resources. The second priority is to improve the accuracy and reliability of management information pertaining to the department's mission-critical assets, including military equipment, real property, and general equipment, and validating improvement through existence and completeness testing. The DOD Comptroller directed the DOD components participating in the FIAR Plan—the departments of the Army, Navy, Air Force and the Defense Logistics Agency—to use a standard process and aggressively modify their activities to support and emphasize achievement of the priorities.

GAO supports DOD's current approach of focusing and prioritizing efforts in order to achieve incremental progress in addressing weaknesses and making progress toward audit readiness. Budgetary and asset information is widely used by DOD managers at all levels, so its reliability is vital to daily operations and management. DOD needs to provide accountability over the existence and completeness of its assets. Problems with asset accountability can further complicate critical functions, such as planning for the current troop withdrawals.

In May 2010, DOD introduced a new phased approach that divides progress toward achieving financial statement auditability into five waves (or phases) of concerted improvement activities (see appendix I). According to DOD, the components' implementation of the methodology described in the 2010 FIAR Plan is essential to the success of the department's efforts to ultimately achieve full financial statement auditability. To assist the components in their efforts, the FIAR guidance, issued along with the revised plan, details the implementation of the methodology with an emphasis on internal controls and supporting documentation that recognizes both the challenge of resolving the many internal control weaknesses and the fundamental importance of establishing effective and efficient financial management. The FIAR Guidance provides the process for the components to follow, through their individual Financial Improvement Plans, in assessing processes, controls, and systems; identifying and correcting weaknesses; assessing, validating, and sustaining corrective actions; and achieving full auditability. The guidance directs the components to identify responsible organizations and personnel and resource requirements for improvement

work. In developing their plans, components use a standard template that comprises data fields aligned to the methodology. The consistent application of a standard methodology for assessing the components' current financial management capabilities can help establish valid baselines against which to measure, sustain, and report progress.

Numerous Challenges Must Be Addressed in Order for DOD to Successfully Reform Financial Management

Improving the department's financial management operations and thereby providing DOD management and the Congress more accurate and reliable information on the results of its business operations will not be an easy task. It is critical that the current initiatives being led by the DOD Deputy Chief Management Officer and the DOD Comptroller be continued and provided with sufficient resources and ongoing monitoring in the future. Absent continued momentum and necessary future investments, the current initiatives may falter, similar to previous efforts. Below are some of the key challenges that the department must address in order for the financial management operations of the department to improve to the point where DOD may be able to produce auditable financial statements.

Committed and sustained leadership. The FIAR Plan is in its sixth year and continues to evolve based on lessons learned, corrective actions, and policy changes that refine and build on the plan. The DOD Comptroller has expressed commitment to the FIAR goals, and established a focused approach that is intended to help DOD achieve successes in the near term. But the financial transformation needed at DOD, and its removal from GAO's high-risk list, is a long-term endeavor. Improving financial management will need to be a cross-functional endeavor. It requires the involvement of DOD operations performing other business functions that interact with financial management—including those in the high-risk areas of contract management, supply chain management, support infrastructure management, and weapon systems acquisition. As acknowledged by DOD officials, sustained and active involvement of the department's Chief Management Officer, the Deputy Chief Management Officer, the military departments' Chief Management Officers, the DOD Comptroller, and other senior leaders is critical. Within every administration, there are changes at the senior leadership; therefore, it is paramount that the current initiative be institutionalized throughout the department—at all working levels—in order for success to be achieved.

Effective plan to correct internal control weaknesses. In May 2009, we reported¹⁶ that the FIAR Plan did not establish a baseline of the department's state of internal control and financial management weaknesses as its starting point. Such a baseline could be used to assess and plan for the necessary improvements and remediation to be used to measure incremental progress toward achieving estimated milestones for each DOD component and the department. DOD currently has efforts underway to address known internal control weaknesses through three interrelated programs: (1) Internal Controls over Financial Reporting (ICOFR) program, (2) ERP implementation, and (3) FIAR Plan. However, the effectiveness of these three interrelated efforts at establishing a baseline remains to be seen. Furthermore, DOD has yet to identify the specific control actions that need to be taken in Waves 4 and 5 of the FIAR Plan, which deal with asset accountability and other financial reporting matters. Because of the department's complexity and magnitude, developing and implementing a comprehensive plan that identifies DOD's internal control weaknesses will not be an easy task. But it is a task that is critical to resolving the long-standing weaknesses and will require consistent management oversight and monitoring for it to be successful.

Competent financial management workforce. Effective financial management in DOD will require a knowledgeable and skilled workforce that includes individuals who are trained and certified in accounting, well versed in government accounting practices and standards, and experienced in information technology. Hiring and retaining such a skilled workforce is a challenge DOD must meet to succeed in its transformation to efficient, effective, and accountable business operations. The National Defense Authorization Act for Fiscal Year 2006¹⁷ directed DOD to develop a strategic plan to shape and improve the department's civilian workforce. The plan was to, among other things, include assessments of (1) existing critical skills and competencies in DOD's civilian workforce, (2) future critical skills and competencies needed over the next decade, and (3) any gaps in the existing or future critical skills and competencies identified. In

¹⁶GAO-09-373.

¹⁷Pub. L. No. 109-163, div. A, § 1122, 119 Stat. 3136, 3452 (Jan. 6, 2006). The National Defense Authorization Act for Fiscal Year 2010 made this strategic plan submission into a permanent annual requirement. Pub. L. No. 111-84, div. A, § 1108, 123 Stat. 2190, 2488 (Oct. 28, 2009), *codified at* 10 U.S.C. § 115b.

addition, DOD was to submit a plan of action for developing and reshaping the civilian employee workforce to address any identified gaps, as well as specific recruiting and retention goals and strategies on how to train, compensate, and motivate civilian employees. In developing the plan, the department identified financial management as one of its enterprisewide mission-critical occupations.

In July 2011, we reported¹⁸ that DOD's 2009 overall civilian workforce plan had addressed some legislative requirements, including assessing the critical skills of its existing civilian workforce. Although some aspects of the legislative requirements were addressed, DOD still has significant work to do. For example, while the plan included gap analyses related to the number of personnel needed for some of the mission-critical occupations, the department had only discussed competency gap analyses for 3 mission-critical occupations—language, logistics management, and information technology management. A competency gap for financial management was not included in the department's analysis. Until DOD analyzes personnel needs and gaps in the financial management area, it will not be in a position to develop an effective financial management recruitment, retention, and investment strategy to successfully address its financial management challenges.

Accountability and effective oversight. The department established a governance structure for the FIAR Plan, which includes review bodies for governance and oversight. The governance structure is intended to provide the vision and oversight necessary to align financial improvement and audit readiness efforts across the department. To monitor progress and hold individuals accountable for progress, DOD managers and oversight bodies need reliable, valid, meaningful metrics to measure performance and the results of corrective actions. In May 2009, we reported¹⁹ that the FIAR Plan did not have clear results-oriented metrics. To its credit, DOD has taken action to begin defining results-oriented FIAR metrics it intends to use to provide visibility of component-level progress in assessment; and testing and remediation activities, including progress in identifying and addressing supporting documentation issues.

¹⁸GAO, *DOD Civilian Personnel: Competency Gap Analysis and Other Actions Needed to Enhance DOD's Strategic Workforce Plans*, GAO-11-827T (Washington, D.C.: July 14, 2011).

¹⁹GAO-09-373.

We have not yet had an opportunity to assess implementation of these metrics—including the components' control over the accuracy of supporting data—or their usefulness in monitoring and redirecting actions.

Ensuring effective monitoring and oversight of progress—especially by the leadership in the components—will be key to bringing about effective implementation, through the components' Financial Improvement Plans, of the department's financial management and related business process reform. If the department's future FIAR Plan updates provide a comprehensive strategy for completing Waves 4 and 5, the plan can serve as an effective tool to help guide and direct the department's financial management reform efforts.

Effective oversight holds individuals accountable for carrying out their responsibilities. DOD has introduced incentives such as including FIAR goals in Senior Executive Service Performance Plans, increased reprogramming thresholds granted to components that receive a positive audit opinion on their Statement of Budgetary Resources, audit costs funded by the Office of the Secretary of Defense after a successful audit, and publicizing and rewarding components for successful audits. The challenge now is to evaluate and validate these and other incentives to determine their effectiveness and whether the right mix of incentives has been established.

Well-defined enterprise architecture. For decades, DOD has been challenged in modernizing its timeworn business systems. Since 1995, we have designated DOD's business systems modernization program as high risk. Between 2001 and 2005, we reported that the modernization program had spent hundreds of millions of dollars on an enterprise architecture and investment management structures that had limited value. Accordingly, we made explicit architecture and investment management-related recommendations. Congress included provisions in the Ronald W. Reagan National Defense Authorization Act for Fiscal Year 2005 that were consistent with our recommendations. In response, DOD continues to take steps to comply with the act's provisions and to satisfy relevant system modernization management guidance. Collectively, these steps address best practices in implementing the statutory provisions concerning the business enterprise architecture and review of systems costing in excess of \$1 million. However, long-standing challenges that we previously identified remain to be addressed. Specifically, while DOD

continues to release updates to its corporate enterprise architecture, the architecture has yet to be federated²⁰ through development of aligned subordinate architectures for each of the military departments. In this regard, each of the military departments has made progress in managing its respective architecture program, but there are still limitations in the scope and completeness, as well as the maturity of the military departments' architecture programs. For example, while each department has established or is in the process of establishing an executive committee with responsibility and accountability for the enterprise architecture, none has fully developed an enterprise architecture methodology or a well-defined business enterprise architecture and transition plan to guide and constrain business transformation initiatives. In addition, while DOD continues to establish investment management processes, the DOD enterprise and the military departments' approaches to business systems investment management still lack the defined policies and procedures to be considered effective investment selection, control, and evaluation mechanisms. Until DOD fully implements these longstanding institutional modernization management controls, its business systems modernization will likely remain a high-risk program.

Successful implementation of the ERPs. The department has invested billions of dollars and will invest billions more to implement the ERPs. DOD officials have said that successful implementation of ERPs is key to transforming the department's business operations, including financial management, and in improving the department's capability to provide DOD management and Congress with accurate and reliable information on the results of DOD's operations. DOD has stated that the ERPs will replace over 500 legacy systems. The successful implementation of the ERPs is not only critical for addressing long-standing weaknesses in financial management, but equally important for helping to resolve weaknesses in other high-risk areas such as business transformation, business system modernization, and supply chain management.

²⁰A federated architecture consists of a family of coherent but distinct member architectures in which subsidiary architectures conform to an overarching corporate architectural view and rule set.

Over the years we have reported²¹ that the department has not effectively employed acquisition management controls to help ensure the ERPs deliver the promised capabilities on time and within budget. Delays in the successful implementation of ERPs have extended the use of existing duplicative, stovepiped systems, and continued funding of the existing legacy systems longer than anticipated. Additionally, the continued implementation problems can erode savings that were estimated to accrue to DOD as a result of modernizing its business systems and thereby reduce funds that could be used for other DOD priorities.

To help improve the department's management oversight of its ERPs, we have recommended²² that DOD define success for ERP implementation in the context of business operations and in a way that is measurable. Accepted practices in system development include testing the system in terms of the organization's mission and operations—whether the system performs as envisioned at expected levels of cost and risk when implemented within the organization's business operations. Developing and using specific performance measures to evaluate a system effort should help management understand whether the expected benefits are being realized. Without performance measures to evaluate how well these systems are accomplishing their desired goals, DOD decision makers, including program managers, do not have all the information they need to evaluate their investments to determine whether the individual programs are helping DOD achieve business transformation and thereby improve upon its primary mission of supporting the warfighter.

Another key element in DOD efforts to modernize its business systems is investment management policies and procedures. We reported in June 2011²³ that DOD's oversight process does not provide sufficient visibility

²¹GAO-10-461; *DOD Business Systems Modernization: Navy Implementing a Number of Key Management Controls on Enterprise Resource Planning System, but Improvements Still Needed*, GAO-09-841 (Washington, D.C.: Sept. 15, 2009); GAO-08-896; GAO-08-866; *DOD Business Systems Modernization: Key Marine Corps System Acquisition Needs to Be Better Justified, Defined, and Managed*, GAO-08-822 (Washington, D.C.: July 28, 2008); GAO-07-860.

²²GAO, *DOD Business Transformation: Improved Management and Oversight of Business Modernization Efforts Needed*, GAO-11-53 (Washington, D.C.: Oct. 7, 2010).

²³GAO, *Department of Defense: Further Actions Needed to Institutionalize Key Business Systems Modernization Management Control*, GAO-11-684 (Washington, D.C.: June 29, 2011).

into the military department's investment management activities, including its reviews of systems that are in operations and maintenance made and smaller investments. As discussed in our information technology investment management framework and previous reports on DOD's investment management of its business systems,²⁴ adequately documenting both policies and associated procedures that govern how an organization manages its information technology projects and investment portfolios is important because doing so provides the basis for rigor, discipline, and repeatability in how investments are selected and controlled across the entire organization. Until DOD fully defines missing policies and procedures, it is unlikely that the department's over 2,200 business systems will be managed in a consistent, repeatable, and effective manner that, among other things, maximizes mission performance while minimizing or eliminating system overlap and duplication. To this point, there is evidence showing that DOD is not managing its systems in this manner. For example, DOD reported that of its 79 major business and other IT investments, about a third are encountering cost, schedule, and performance shortfalls requiring immediate and sustained management attention. In addition, we have previously reported²⁵ that DOD's business system environment has been characterized by (1) little standardization, (2) multiple systems performing the same tasks, (3) the same data stored in multiple systems, and (4) manual data entry into multiple systems. Because DOD spends billions of dollars annually on its business systems and related IT infrastructure, the potential for identifying and avoiding the costs associated with duplicative functionality across its business system investments is significant.

Closing Comments

In closing, I am encouraged by the recent efforts and commitment DOD's leaders have shown toward improving the department's financial management. Progress we have seen includes recently issued guidance

²⁴GAO, *Business Systems Modernization: DOD Needs to Fully Define Policies and Procedures for Institutionally Managing Investments*, GAO-07-538 (Washington, D.C.: May 11, 2007); *Business Systems Modernization: Air Force Needs to Fully Define Policies and Procedures for Institutionally Managing Investments*, GAO-08-52 (Washington D.C.: Oct. 31, 2007); *Business Systems Modernization: Department of the Navy Needs to Establish Management Structure and Fully Define Policies and Procedures for Institutionally Managing Investments*, GAO-08-53 (Washington, D.C.: Oct. 31, 2007).

²⁵GAO, *Opportunities to Reduce Potential Duplication in Government Programs, Save Tax Dollars, and Enhance Revenue*, GAO-11-318SP (Washington, D.C.: Mar. 1, 2011).

to aid DOD components in their efforts to address their financial management weaknesses and achieve audit readiness; standardized component financial improvement plans to facilitate oversight and monitoring; and the sharing of lessons learned. In addition, the DCMO and the DOD Comptroller have shown commitment and leadership in moving DOD's financial management improvement efforts forward.

The revised FIAR strategy is still in the early stages of implementation, and DOD has a long way and many long-standing challenges to overcome, particularly with regard to sustained commitment, leadership, and oversight, before the department and its military components are fully auditable, and DOD financial management is no longer considered high risk. However, the department is heading in the right direction and making progress. Some of the most difficult challenges ahead lie in the effective implementation of the department's strategy by the Army, Navy, Air Force, and DLA, including successful implementation of ERP systems and integration of financial management improvement efforts with other DOD initiatives.

GAO will continue to monitor the progress of and provide feedback on the status of DOD's financial management improvement efforts. We currently have work in progress to assess implementation of the department's FIAR strategy and efforts toward auditability.

As a final point, I want to emphasize the value of sustained congressional interest in the department's financial management improvement efforts, as demonstrated by this Panel's leadership.

Mr. Chairman and Members of the Panel, this concludes my prepared statement. I would be pleased to respond to any questions that you or other members of the Panel may have at this time.

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Appendix I: FIAR Plan Waves

The first three waves focus on achieving the DOD Comptroller's interim budgetary and asset accountability priorities, while the remaining two waves are intended to complete actions needed to achieve full financial statement auditability. However, the department has not yet fully defined its strategy for completing waves 4 and 5. Each wave focuses on assessing and strengthening internal controls and business systems related to the stage of auditability addressed in the wave.

Wave 1—Appropriations Received Audit focuses on the appropriations receipt and distribution process, including funding appropriated by Congress for the current fiscal year and related apportionment/reapportionment activity by the OMB, as well as allotment and sub-allotment activity within the department.

Wave 2—Statement of Budgetary Resources Audit focuses on supporting the budget-related data (e.g., status of funds received, obligated, and expended) used for management decision making and reporting, including the Statement of Budgetary Resources. In addition to fund balance with Treasury reporting and reconciliation, other significant end-to-end business processes in this wave include procure-to-pay, hire-to-terminate, order-to-cash, and budget-to-report.

Wave 3—Mission Critical Assets Existence and Completeness Audit focuses on ensuring that all assets (including military equipment, general equipment, real property, inventory, and operating materials and supplies) that are recorded in the department's accountable property systems of record exist; all of the reporting entities' assets are recorded in those systems of record; reporting entities have the right (ownership) to report these assets; and the assets are consistently categorized, summarized, and reported.

Wave 4—Full Audit Except for Legacy Asset Valuation includes the valuation assertion over new asset acquisitions and validation of management's assertion regarding new asset acquisitions, and it depends on remediation of the existence and completeness assertions in Wave 3. Also, proper contract structure for cost accumulation and cost accounting data must be in place prior to completion of the valuation assertion for new acquisitions. It involves the budgetary transactions covered by the Statement of Budgetary Resources effort in Wave 2, including accounts receivable, revenue, accounts payable, expenses, environmental liabilities, and other liabilities.

Wave 5—Full Financial Statement Audit focuses efforts on assessing and strengthening, as necessary, internal controls, processes, and business systems involved in supporting the valuations reported for legacy assets once efforts to ensure control over the valuation of new assets acquired and the existence and completeness of all mission assets are deemed effective on a go-forward basis. Given the lack of documentation to support the values of the department's legacy assets, federal accounting standards allow for the use of alternative methods to provide reasonable estimates for the cost of these assets.

In the context of this phased approach, DOD's dual focus on budgetary and asset information offers the potential to obtain preliminary assessments regarding the effectiveness of current processes and controls and identify potential issues that may adversely impact subsequent waves.

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DOCUMENTS SUBMITTED FOR THE RECORD

JULY 28, 2011

House Committee on Armed Services
Panel on Defense Financial Management and Auditability Reform
Organizational Plan

Panel Members

Mike Conaway, TX, Chairman	Robert Andrews, NJ, Ranking Member
Scott Rigell, VA	Joe Courtney, CT
Steve Palazzo, MS	Tim Ryan, OH
Todd Young, IN	

Rules and Procedures

The panel is constituted under Rule 5(a) of the rules of the Committee on Armed Services to serve for a period of six months beginning on the date of its organization, July 13, 2011. The Chairman of the Committee has the discretion to reappoint the panel for a period of time that may extend to an additional six months.

The panel will follow the rules and procedures of the House Armed Services Committee, as adopted by the Committee for the 112th Congress, in all of its meetings, hearings, and other activities.

The panel has been tasked to examine the Department of Defense's financial management system and possible ways to improve its financial management and audit readiness effort. Although it does not have legislative jurisdiction, the panel will report its findings including any recommendations for possible legislation to the Committee.

Staffing

The panel will be assisted by staff of the House Armed Services Committee designated by the Chairman and Ranking Member of the Committee for this purpose.

Work Plan

The Panel will examine the effectiveness of the Department of Defense's (DOD) financial management system to deliver timely, reliable, and useful information for decision making and reporting. In doing so, the panel will evaluate: (1) the challenges to achieving financial management reform and auditability and (2) DOD's efforts to resolve these issues.

In examining DOD's financial management system, the panel will focus on six primary areas:

1. Are DOD's financial improvement and audit readiness strategy and methodology appropriate?
 - a. Is the goal of audit readiness by 2017 not aggressive enough or too aggressive?
 - b. Do the strategy and methodology sufficiently address the necessary steps for achieving financial improvement and audit readiness?
 - c. Does DOD have a realistic approach to achieve auditability on the full set of financial statements (which includes asset valuation) by 2017?
 - d. How do DOD's organizational structure and many diverse functional areas present challenges to achieving audit readiness?
2. Is DOD effectively implementing its financial improvement and audit readiness strategy and methodology?
 - a. Is DOD making progress in achieving its short-term and long-term audit readiness milestones?
 - b. Do DOD and its components have the appropriate level of resources to implement the financial improvement and audit readiness effort?
 - c. What are the factors preventing DOD from being auditable?
 - d. Have lessons learned from audits of DOD components (e.g. the USMC Statement of Budgetary Resources audit and the Army Corps of Engineers audit) been implemented by other components?
3. Are the Enterprise Resource Planning (ERP) efforts addressing DOD's fundamental financial management weaknesses?
 - a. How is implementation of ERP intended to improve DOD's financial management?
 - b. What is the scope required for DOD's ERP efforts?
 - c. What are the resources required for DOD's ERP efforts?
 - d. What is the impact of the ERP delays and cost overruns on DOD financial management reform and audit readiness milestones?
4. Does DOD's financial management workforce (including those individuals involved in the audit readiness effort) have the appropriate skills, incentives, and numbers needed for effective financial management?
5. What changes are necessary to ensure that DOD improves its financial management, including removing the financial management area from the GAO high risk list, and achieves audit readiness as quickly as practicable?
6. What congressional action may be needed to help DOD improve its financial management and achieves audit readiness by 2017?

In addition to these matters, the panel may examine other issues related to DOD's financial management system at the request of the Committee's Chairman with the concurrence of the Committee's Ranking Member.

**WITNESS RESPONSES TO QUESTIONS ASKED DURING
THE HEARING**

JULY 28, 2011

RESPONSE TO QUESTION SUBMITTED BY MR. RIGELL

Secretary HALE. While the outside auditors have provided feedback on the audits, they have not made any legislative suggestions. The auditors' detailed observations and recommendations from the financial statement audit of the U.S. Marine Corps (USMC) General Fund Statement of Budgetary Resources (SBR) follow.

The audit has yielded significant improvements in key business processes and internal controls. The Fiscal Year (FY) 2010 audit employed a two-track approach to assessing the validity and fair presentation of General Fund SBR in accordance with accounting principles generally accepted in the U.S. (GAAP). Audit work streams were segmented into two distinct categories: 1) Financial Transaction Supportability; and 2) Information Systems Reliability.

Financial Transaction Supportability—Audit requirements are aimed at supporting the balances reported on the financial statement by performing examination procedures that tie the accounting transaction to its corresponding supporting documentation. These are termed “substantive procedures” and assume little, if any, reliance on internal controls.

The auditors approached testing across three key components of the financial statement: 1) Beginning Balances; 2) Current-Year Operations; and 3) Ending Balances and Compilation. The most difficult and challenging component of a first-year audit is assessing the reliability of a Beginning Balance, which represents all brought forward balances for every appropriation that is not in cancelled status in the year of audit. That is, appropriations that are active for making obligation adjustments and/or disbursement for requirements established in a prior period and remain active. The USMC financial statement audit did not significantly progress beyond Beginning Balance testing in FY 2010 because of the following significant auditor observations and findings:

1. **Inappropriate Accrual.** The auditors uncovered inappropriate accruals that lacked support at the time of recognition and entry into the core accounting system. This matter was corrected by the USMC prior to the end of the FY 2010 SBR audit.
2. **Lack of Management Evidence to Substantiate Obligation Estimates.** On occasion, the USMC initiates a “bulk” transaction or one that is based on an estimate or calculation for future requirements. The auditors determined that these estimates were not being monitored or adjusted as necessary. As a result of this audit finding, the USMC has taken steps to implement improved estimation models and monitoring controls.
3. **Inappropriate Recognition of Contract Financing Payments as Advances.** The auditors confirmed the equal general ledger treatment of advances (pre-payments) and contract financing payment. This represents an accounting classification error for a specific subset of assets. Although the USMC has corrected its core accounting system logic in order to properly record and report contract financing payments, the impact of this issue to the balances reflected on the financial statement was minimal. Prior to the SBR audit, the USMC was in compliance with the *Department of Defense Financial Management Regulation (DoDFMR)* when processing the recognition of contract financing payments. However, as a result of this audit, there are efforts underway within the Office of the Under Secretary of Defense (Comptroller) to update and clarify the DoDFMR.
4. **Timely Recording and Review.** The auditors identified a number of documents during testing that contained abnormal balances. These balances were a combination of negative obligations, latent undelivered orders balances, documents containing no recorded expenses, and stale obligations. A more robust quarterly and year-end review is needed in order to maintain normal balances on the documents in the core accounting system. This includes stronger management oversight and review of monthly reporting. The USMC has strengthened the tri-annual review process that is required throughout the DoD.

5. **Trial Balance Compilation.** The compilation and reconciliation of the detailed transactions to the financial statements is the first and most important requirement of any audit. The USMC was able, although with some difficulty and delay, to reconcile the detailed financial transactions to the unadjusted trial balance that the auditors use to sample and test the balances of the SBR. In order to sustain these improvements, the USMC implemented a series of reports that are generated monthly to facilitate faster and more accurate data exchange to the auditors. Additionally, the USMC worked closely with the Defense Finance and Accounting Service (DFAS) and the Business Transformation Agency to create a complete general ledger reconciliation of the unadjusted trial balance to the adjusted trial balance. This was an achievement never accomplished prior to the audit that spurred improved financial reporting and reconciliation support that will yield tangible audit benefits all financial statement reporting entities within the DoD.
6. **Shared Appropriations.** Shared appropriations are appropriations identified and authorized through the Department of the Navy (DON) annual budget process that are shared by the Navy and the USMC. The auditors uncovered the inappropriate use of a general ledger account that does not reflect an allotment from the DON. For the FY 2011 General Fund SBR audit, the USMC implemented general ledger corrections to effect a reclassification across the impacted general ledger accounts to support the appropriate recording and reporting of a shared appropriation. There is no net effect to the presentation of the financial statement and the balances reported. These corrections are currently under evaluation.

Information Systems Reliability—The audit requirements focus on leveraging the Government Accountability Office Federal Information System Controls Audit Manual in the auditor's approach for testing financial systems and mixed-use systems controls. The controls tested consisted of select internal controls that depend on information systems processing and included general controls and application controls.

The FY 2010 audit focused on three systems: 1) the Marine Corps Total Force System (MCTFS); 2) the Standard Accounting Budgeting and Reporting System (SABRS); and 3) the Defense Departmental Reporting System (DDRS). Of the three systems, only one system, MCTFS, is owned by the USMC. MCTFS supports integrated personnel and pay transactions for both the active and reserve components of the USMC as well as retired Marines. SABRS, which is owned by DFAS, is the core accounting systems used by the USMC for all General Funds appropriations. DDRS is used by the USMC to produce DoD financial statements, interim financial statements and budgetary reports. For FY 2011, the auditors added the Defense Cash Accountability System (DCAS) to their information systems audit scope. Along with DDRS, audit assessment of DCAS represents significant value for the DoD as this is a key financial recording and reporting system that is utilized across the enterprise.

The FY 2010 audit of the USMC SBR identified 56 information systems (IS) audit findings for the 3 systems. Examples of the auditor's observations and findings, as categorized by application control, include:

1. **Security Management.** These controls provide reasonable assurance that security management is effective. The auditors identified instances where application level logging and monitoring was not performed and formal policy and procedures for the monitoring performed by third party providers had not been documented. By not actively monitoring application level activity nor third party providers adherence to service level agreements or other performance metrics, management cannot ensure they are receiving the agreed upon services at agreed upon metrics. There is also the risk that the third party provider does not properly communicate any security vulnerability to management in a timely manner. This could impact the SBR if unauthorized, fraudulent, or erroneous application activity is not detected, logged, and investigated by the third-party information technology (IT) security organization.
2. **Access Controls.** These controls provide reasonable assurance that access to computer resources (data, equipment, and facilities) is reasonable and restricted to authorized individuals. The audit revealed that periodic management review of user access was not performed. Without periodic reviews and recertification of users, inappropriate access to significant financial data may be undetected. Additionally, there is risk of lingering access for employees who have been reassigned, terminated, or retired.

3. Configuration Management. These controls provide reasonable assurance that changes to information system resources are authorized and systems are configured and operated securely and as intended. The audit revealed little evidence of periodic review of changes that were migrated into production. Without a periodic review of changes that are migrated to production, there is an increased risk that an unauthorized, erroneous, or harmful code could be introduced the production environment and negatively impact the SBR financial statement reporting systems and related processes.
4. Segregation of Duties. These controls provide reasonable assurance that incompatible duties are effectively segregated. The auditors uncovered instances where administrators were granted a functional role for their administrator accounts without an approved waiver from management. By not effectively restricting access to applications based on job function and adhering to segregation of duties principles, the risks for fraud and inappropriate transactions are increased.
5. Contingency Planning. These controls provide reasonable assurance that contingency planning: 1) protects information resources and minimizes the risk of unplanned interruptions; and 2) provides for recovery of critical operations should interruptions occur. The contingency plan was not approved or tested, and did not include a business impact analysis. By not having a tested contingency plan and business impact analysis, there is an increased risk that the USMC will not be able to restore a system quickly and effectively after a service disruption.
6. Business Process. These controls are the automated and/or manual controls applied to business transaction flows. They relate to the completeness, accuracy, validity and confidentiality of transactions and data during application processing. They typically cover the structure, policies, and procedures that operate at a detailed business process level and operate over individual transactions or activities across business processes. The auditors found that a data management strategy and design (i.e., how data is organized into structures to facilitate retrieval while minimizing redundancy) was not formally documented. Additionally, there was no formal procedure that documented how data was managed and monitored. A data management strategy and design is a critical factor in helping to assure the quality of data as well as its interrelationship with other data elements. Without a data management strategy and design there is a risk of poor quality data that may lead to a failure of system controls, process inefficiencies, and inaccurate management reporting.
7. Interface Controls. These consist of those controls over the: 1) timely, accurate, and complete processing of information between applications and other feeder and receiving systems on an on-going basis; and 2) complete and accurate migration of clean data during conversion. Documentation that identified, listed, and provided an explanation for interface data processing files was not readily available for the auditors. Without properly listing, identifying, and providing an explanation for all the edit conditions contained in the input process program, there is no evidence that the edit checks are appropriately configured for data processing.
8. Data Management System Controls. Enforce user authentication/authorization, availability of system privileges, data access privileges, application processing hosted within the data management systems, and segregation of duties. The audit testing found that multiple users shared one administrative account and password to access the Collection Server and could invoke privileged level access. Allowing the use of a shared account decreases the ability for management to establish accountability for user actions. Additionally, the use of a guest account with administrative privileges compounds the potential effect by having a generic account that could potentially be used to modify system settings or data without the action being tied to an individual.

The audit helped to identify areas of both financial and IS risk in the USMC. The USMC audit team has worked with the auditors to understand the issues and risks and has taken firm action to remediate the known findings. The corrective actions resulting from the findings and issues identified in the FY 2010 audit are currently being reevaluated by the auditors during the FY 2011 audit. At this time the FY 2011 audit is not complete. The USMC is confident that its action to address these audit issues and findings in FY 2011 will be sustained and ultimately validated by an audit opinion. Additionally, the USMC will continue to strengthen its manage-

ment controls and improve its IT security posture in response to any future audit findings. [See page 16.]

QUESTIONS SUBMITTED BY MEMBERS POST HEARING

JULY 28, 2011

QUESTIONS SUBMITTED BY MR. PALAZZO

Mr. PALAZZO. On Page 7, under the heading "Where We Are Today," you stated that you are "assembling teams within each Military Department that will be tasked with improving financial controls." I applaud your efforts to assemble these important teams within the Services. Can you please elaborate, for the Panel, the makeup of these teams with respect to their accounting background? How many of them are working on this task daily, etc?

Secretary HALE and Ms. MCGRATH. Congressman Palazzo let me start by thanking you for your comment in support of our plan to assemble teams to improve financial controls. Our plan calls for each Military Department to devote at least 15 people from its audit agency to assist the Department to improve its internal controls. Auditors have the experience needed to assist business and financial process owners with designing sound internal controls and then assisting with their effective implementation. As for the accounting background of the teams, the employment requirements for auditors include at least 24 hours of accounting or auditing course work and many of the auditors have years of financial audit experience.

Mr. PALAZZO. On Page 5 of your submitted statement, you mention that the "Deputy Secretary has made clear that one of his highest management priorities is improving the acquisition, development, and fielding of IT systems." While I can appreciate the attention and urgency given to acquiring, developing, and getting IT systems into the field, could DOD utilize systems they already have, instead of going through rounds of acquisitions to purchase something we could find in a desk drawer?

Secretary HALE and Ms. MCGRATH. The Department is committed to taking a balanced approach to transitioning from its legacy systems environment to its target systems environment. This balanced approach includes both the acquisition of new systems and the modernization or retirement of existing systems. In many cases, utilization of existing systems to meet current capability needs is not possible, however, due to outdated programming languages, non-compliance with statute such as the Federal Financial Management Improvement Act (FFMIA), stovepiped business processes, or a variety of other reasons. In those cases, it is critical that the Department efficiently and effectively acquire new business systems that help to integrate our business operations and deliver interoperable data.

