



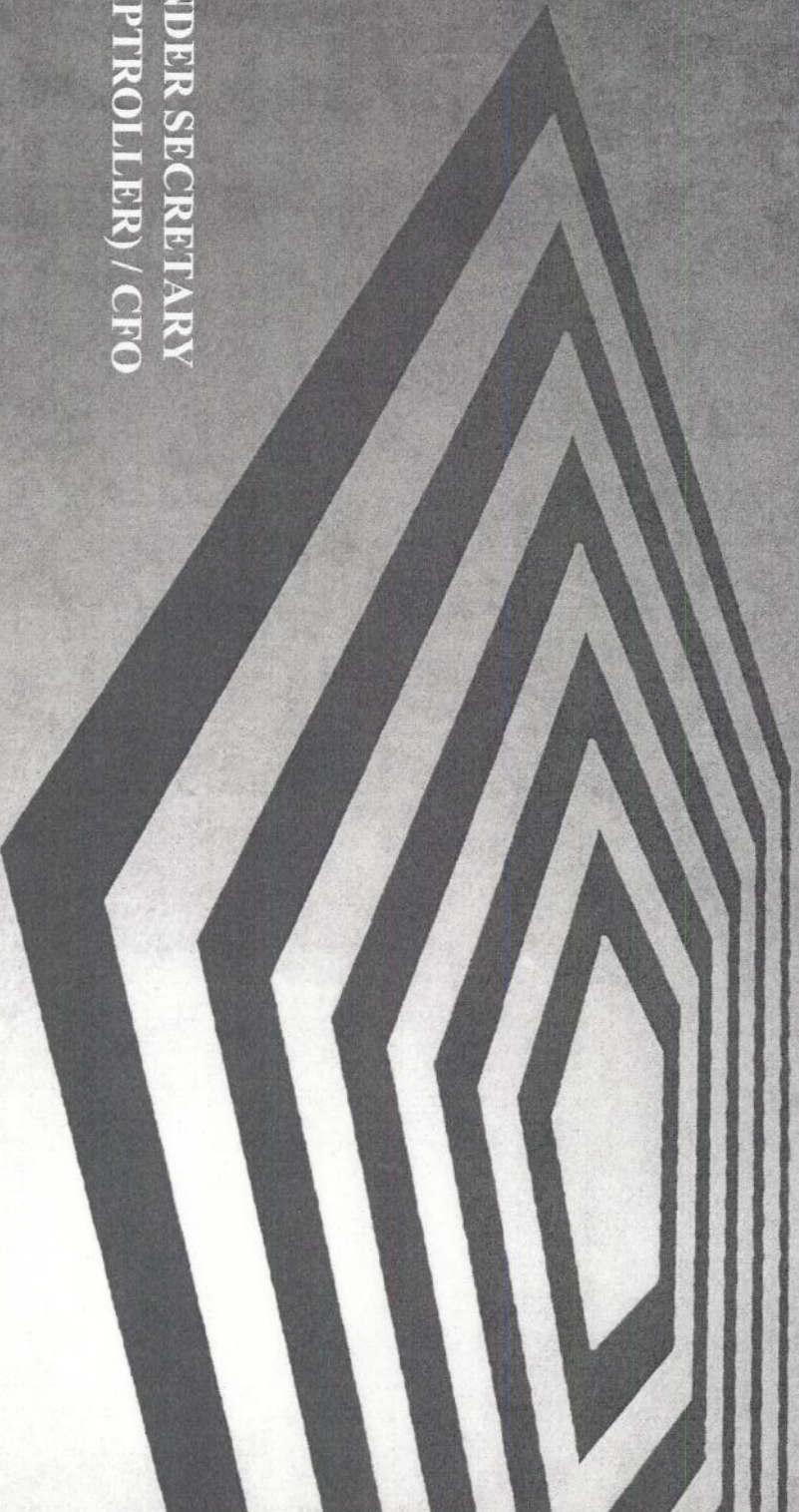
UNITED STATES DEPARTMENT OF DEFENSE

FINANCIAL IMPROVEMENT AND AUDIT READINESS (FIAR) PLAN

Status Report

May 2010

OFFICE OF THE UNDER SECRETARY
OF DEFENSE (COMPTROLLER) / CFO



Message from the Under Secretary of Defense (Comptroller)

Today, approximately 50,000 men and women serve as financial managers in the Department of Defense (DoD). They serve at almost every DoD location, including those in Iraq and Afghanistan. I believe that these men and women are successfully helping the Department accomplish its critical national security mission, and I am proud of their efforts.

To assist in accomplishing the DoD mission, we need to continue to improve the Department's financial processes, controls and information. The Financial Improvement and Audit Readiness (FIAR) Plan outlines the strategy, priorities and methodology for achieving these objectives. A cornerstone of the FIAR Plan is the newly formulated strategy focusing improvement efforts on information important to DoD management. This strategy focuses our work on budgetary information and information on mission critical assets. This FIAR Plan Status Report provides the status of the major components of our new strategy and plans for achieving them.

We have made progress over the past year due primarily to the unwavering, collaborative efforts of numerous individuals and organizations across the Department. I am confident that progress will continue due to the increased resources we have applied to these efforts and because our current plans focus on the financial information most needed to manage the Department.



Robert F. Hale

Under Secretary of Defense (Comptroller)

Table of Contents

CONTENTS

MESSAGE FROM THE UNDER SECRETARY OF DEFENSE (COMPTROLLER)

TABLE OF CONTENTS..... i

EXECUTIVE SUMMARY 1

I. THE FIAR STRATEGY 8

II. FY 2010 NDAA REQUIRED INFORMATION 19

III. AUDIT READY STATEMENT OF BUDGETARY RESOURCES (WAVE 1 & WAVE 2)..... 21

IV. AUDIT READY EXISTENCE AND COMPLETENESS OF ASSETS (WAVE 3) 41

APPENDIX 1. FIAR AUDIT READINESS STRATEGY AND METHODOLOGY..... A1-1

APPENDIX 2. NDAA FOR FISCAL YEAR 2010 REQUIRED INFORMATION..... A2-1

APPENDIX 3. STATEMENT OF BUDGETARY RESOURCES COMPOSITION..... A3-1

APPENDIX 4. COMMONLY USED ACRONYMS..... A4-1

Executive Summary

This Report was prepared in accordance with Section 1003 of the National Defense Authorization Act (NDAA) for Fiscal Year (FY) 2010 and provides the status of the Department's progress in achieving the goals of the Financial Improvement and Audit Readiness (FIAR) Plan. As directed by the NDAA, it also describes (in Section II) the actions taken and planned to implement specific requirements of the Act.

The FIAR Plan serves to advance the Department's fiscal stewardship by organizing, prioritizing and monitoring the financial improvement efforts of the Military Departments and Defense Agencies. The goals of the FIAR Plan focus improvements on business and financial processes, controls, systems and data to achieve accurate, reliable and timely financial information for decision makers validated by successful financial statement audits.

Since 2005, when the FIAR Plan was first issued, much has been accomplished to improve financial management across the Department of Defense (DoD); however, much remains to be done. Although DoD cannot produce auditable financial statements today, the Department effectively manages its budgets, appropriations and expenditures, as verified by its ability to provide financial support for two wars and, more specifically, by measures contained in this Report (Progress Metrics in Sections III and IV).

PROGRESS MADE BUT CHALLENGES REMAIN

In recent years, the Department has made measured progress in improving financial information and in achieving audifiability, as demonstrated by:

- FY 2009 Financial Statement unqualified audit opinions:
 - U.S. Army Corps of Engineers - Civil Works
 - Defense Contract Audit Agency (DCAA)
 - Defense Commissary Agency (DeCA)

- Defense Finance and Accounting Service
- Office of the Inspector General
- Military Retirement Fund
- FY 2009 Qualified audit opinions:
 - Medicare-Eligible Retiree Health Care Fund (MERHCF)
 - TRICARE Contract Resource Management
- Validated as audit ready or under audit:
 - Navy Ships Environmental Liabilities
 - Air Force Appropriations Received and Non-expenditure Transfers
 - U.S. Marine Corps (USMC) Statement of Budgetary Resources

The organizations with unqualified audit opinions received more than \$101 billion in budgetary resources in FY 2009, which is more than the budgetary resources under audit in 13 of the 24 individual Chief Financial Officers (CFO) Act Federal agencies.

Of considerable importance is the progress toward audit readiness the Department of the Navy (DON) has achieved, as demonstrated by the ongoing audit of the USMC Statement of Budgetary Resources (SBR). This is the first audit of a Military Service's financial statement. It is the direct result of the commitment made by DON and USMC senior leaders. It also results from the tireless efforts of many people who improved business processes and corrected control deficiencies to prepare for the audit. Lessons learned from the USMC SBR audit will be of great value, not only for the DON and USMC, but for the rest of the Department.

Although progress has been made, significant challenges remain on the road to improving financial information and attaining audit readiness (i.e., the ability to obtain and sustain unqualified financial statement audit opinions). Until recently, the Military Departments and Defense

Agencies were not all pursuing the same priorities, nor had the Department established realistic milestones and provided the resources needed to achieve them.

Most importantly, the Department was pursuing some improvements to financial information as required by law, but was not focusing on the information most useful to managers. As a result, there was not a strong business case for some FIAR activities. Valuation of military equipment is a good example. Attempts to value military equipment have already consumed substantial resources, and efforts to complete the task will be very expensive and time-consuming. However, historical costs of military equipment almost never influence Defense decisions. To varying degrees, this same issue affects all valuation efforts and applies to a number of the financial statements currently required by law and Federal accounting standards.

As a result of this reassessment, the Under Secretary of Defense (Comptroller) (USD(C)) made significant changes to the FIAR objectives and priorities.

SIGNIFICANT CHANGES HAVE BEEN MADE

Over the years since the first FIAR Plan was issued, the strategy and approach have evolved. However, with the recent change in Administration and new DoD senior leadership, the FIAR Plan has changed significantly. The most significant change was made in August 2009, when the USD(C) established new priorities that first focus improvement work on processes and controls supporting information that is most often used to manage the Department. To achieve that objective, the USD(C) designated two priorities:

- Budgetary information, and
- Mission critical asset information.

The USD(C) also directed the Components to aggressively modify their Financial Improvement Plans (FIPs) to address these priorities. The individual Component FIPs, when summarized collectively, are the Department's FIAR Plan. The results of the Components' efforts to

update their FIPs are reflected in this Report. The Components' plans continue to be modified, while work commences on the priorities. The November 2010 FIAR Plan Status Report will provide additional and more detailed information filling gaps that presently exist in the Components' plans. The Department also will add plans for organizations not yet reflected in the FIAR Plan.

Other significant changes have been made to the FIAR Plan and are explained in Section I of this Report. These include:

- Increased resources,
- Clarified goals,
- Focused objectives and priorities,
- Revised audit readiness strategy,
- More detailed, phased methodology, and
- Increased governance by involving the Department's Chief Management Officers.

Although all of these changes are important and affect the Department's ongoing and planned FIAR efforts, increasing resources for financial improvement will have the most impact on progress. Resources for financial improvement and audit readiness activities have competed with other high priorities, such as the Overseas Contingency Operations, resulting in limited funding for FIAR requirements. Lack of resources has been a serious impediment to FIAR progress except in the Navy and DLA, which have been more successful at budgeting for financial improvement efforts, and where more progress has been made compared to the other Components.

The Department's new leadership addressed the unfunded FIAR resource requirements, and funding was increased in the Army and Air Force. Air Force resources are structured to reflect the rollout of their Enterprise Resource Planning (ERP) systems and include a larger proportion of organic government civilian personnel, which lowers cost relative to contractor-focused efforts.

Figure 1. FY 2010 – FY 2014 FIAR Budget

	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
OUSD(C)	\$ 8	\$ 9	\$ 9	\$ 9	\$ 9
Army	9	43	45	61	63
Navy	61	63	65	67	69
Air Force	20	28	27	25	25
DLA	52	45	47	44	45
Totals	\$ 150	\$ 188	\$ 193	\$ 206	\$ 211

Notes: (1) Dollars are in millions. (2) Amounts do not include funds for systems modernization (e.g., ERPs). (3) Navy amounts include funds for audits. (4) DLA amounts include Service Provider audit readiness support. (5) Air Force amounts exclude some organic, field-level support.

The financial improvement activities funded by the budgets in Figure 1 include assistance and oversight by the Office of the USD(C) FIAR Directorate; performing evaluation and discovery; defining, designing and implementing an audit ready environment; documenting, modifying or implementing new processes and controls; testing and strengthening controls; validating and ensuring the availability of supporting transaction documentation; data cleansing; and asserting audit readiness. The Navy amounts also include funds for audits while DLA amounts include funds for Service Provider audit readiness support.

The amounts identified in Figure 1 do not include budgets for systems modernization.

FIAR STATUS AND LONG-TERM AND INTERIM MILESTONES

The amount of work to be done by the Military Departments and Defense Agencies to correct long-standing material weaknesses, test and strengthen controls, and modernize business and financial processes and systems is enormous. It requires an incremental and prioritized strategy and phased methodology with visibility of ongoing and planned actions by those executing the FIPs and those overseeing their execution. To overcome these challenges and focus the

Department’s limited financial improvement resources on the prioritized objectives, the FIAR Strategy, explained in Section I, aligns improvement work into three waves. The three waves are:

- Wave 1 – Appropriations Received Audit
- Wave 2 – Statement of Budgetary Resources (SBR) Audit
- Wave 3 – Mission Critical Asset Existence and Completeness Audit

These three waves concentrate improvement work on the USD(C) directed priorities to improve budgetary and mission critical asset information. Figure 2 provides the current status and milestones for these waves, and when each Component’s Enterprise Resource Planning (ERP) system will achieve full operational capability and complete deployment to the point necessary to achieve auditability. Deployment may continue beyond the milestones shown for varying reasons to include increasing an ERP’s functionality by implementing additional modules to improve business operations. The ERP milestones are included in this figure because the auditability goals of Wave 2, as well as Wave 4 and Wave 5 (described in Appendix 1), are dependent on the successful deployment of the ERPs. The exception to this is the DON, whose current plans do not reflect a dependency on an ERP to achieve an auditable SBR.

In December 2009, the USD(C) directed the Components to resolve deficiencies, strengthen controls and achieve audit readiness by the end of FY 2010 for Wave 1, Appropriations Received, which is the Budget Authority Appropriations line on the SBR. Accordingly, the Components adjusted their FIPs and are presently working to achieve that goal. As indicated in Figure 2, the Navy and Air Force have asserted audit readiness for Wave 1. The OIG has validated the Air Force’s assertion. The Army and Defense Logistics Agency (DLA) will assert audit readiness as of the fourth quarter of this fiscal year.

As shown in Figure 2, the Army is planning to assert audit readiness for the SBR in the first quarter of FY 2015. The Navy is planning to assert SBR audit readiness in the first quarter of FY 2013. The Air

Force is planning to assert SBR audit readiness in the fourth quarter of FY 2016, and DLA's plan reflects the fourth quarter of FY 2017 pending completion of the Evaluation and Discovery phase of its end-to-end business processes.

Other than DLA, Figure 2 does not reflect the plans of any other Defense Agencies or organizations. The Department has analyzed the composition of the DoD Combined SBR to determine all Defense Agencies and other Defense organizations that materially impact the SBR and has begun working with many of them to achieve the objectives of Wave 2. At the time of this Report, the other Defense Agencies and organizations do not have FIPs that conform to the FIAR

Audit Readiness Strategy and Methodology. The November 2010 FIAR Plan Status Report will be more inclusive of all Defense organizations that must be included in order to achieve auditability of the DoD Combined SBR.

In Wave 2, the Army, Navy and Air Force are focusing on the General Fund SBR, while DLA is working both General Fund and Working Capital Fund. The Components are working Wave 2 incrementally by first focusing on specific SBR lines and business processes, referred to as assessable units. Their incremental progress and interim milestones (defined as progress that can be accomplished by the end of FY 2012) are reflected in Figure 3.

Figure 2. Audit Readiness Wave and ERP Milestones

Wave / Component	FY10		FY11		FY12		FY13		FY14		FY15		FY16		FY17		Legend	
	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2		3
Wave 1 - Appropriations Received Audit																		
Army																		
Navy																		
Air Force																		
DLA																		
<i>(Completion Date to Be Provided in November 2010 FIAR Plan Status Report)</i>																		
Wave 2 - Statement of Budgetary Resources Audit																		
Army																		
Navy																		
Air Force																		
USMC																		
DLA**																		
<i>(Completion Date to Be Provided in November 2010 FIAR Plan Status Report)</i>																		
Wave 3 - Mission Critical Asset Existence and Completeness Audit																		
Army																		
Navy																		
Air Force																		
DLA																		
<i>(Completion Date to Be Provided in November 2010 FIAR Plan Status Report)</i>																		
Enterprise Resource Planning (ERP) Systems																		
Army - GFEBBS																		
Army - LMP																		
Army - GCSS-A																		
Navy ERP																		
USMC - GCSS-MC																		
Air Force - DEAMS (incr.1) ¹																		
Air Force - DEAMS (incr.2) ²																		
Air Force - DEAMS (incr.3) ³																		
Air Force - ECSS (Release 1)																		
Air Force - ECSS																		
DLA - Energy Convergence																		

** ODOs are other Defense organizations comprising the remainder of DoD material reporting entities.
 ** DLA's plan reflects the fourth quarter of FY 2017 pending completion of the Discovery phase of its end-to-end business processes.
 1 DEAMS Increment 1 - Implementation at Scott AFB including 2 GSUs (full functionality)
 2 DEAMS Increment 2 - Roll-out to USTC, MSC, SDDC, AMC, ACC, USAFE, PACAF, AFSOC, AETC and AFRC
 3 DEAMS Increment 3 - Roll-out to ASSPC and AFMC
 Note: Wave 3 dates are based on achieving Existence and Completeness audit readiness for all mission critical assets.

Legend

- Audit Readiness Assertion
- Validation Under Audit or Sustainment
- Full Operational Capability
- Deployment

Figure 3. Interim Audit Readiness Goals

Component	Goals	FY 10			FY 11				FY 12				Legend
		3	4	1	2	3	4	1	2	3	4		
USACE, DCAA, DFAS, DeCA, MERHCF, MFR, TRICARE-CRM, OIG	Sustain Audit Opinions												
USMC	Achieve and Sustain SBR Audit Opinion												
Wave 1 - Appropriations Received Audit	Achieve, Validate and Sustain Audit Readiness												
Army & DIA	Achieve, Validate and Sustain Audit Readiness												
Navy	Validate and Sustain Audit Readiness												
Air Force	Sustain Audit Readiness												
Wave 2 - Statement of Budgetary Resources Audit	Achieve, Validate and Sustain Incremental Audit Readiness												
Navy	Military Pay												
	Civilian Pay												
	OM&S - MILSTRIP Orders												
	Contracts												
	Net Outlays (Includes FBWT)												
Air Force	FBWT Reconciliation												
DLA	FBWT												
Wave 3 - Mission Critical Assets Existence and Completeness Audit	Achieve, Validate and Sustain Incremental Audit Readiness												
Army	Military Equipment (4 Asset Types)												
	Fire and Rescue												
Navy	Military Equipment (Ships, Aircraft, (CBMs, Satellites)												
	Military Equipment												
	OM&S - Missile Motors												
	OM&S - Spare Engines												
Air Force	OM&S - Cruise Missiles & Drones												

Figures 2 and 3 also provide the current status and plans for improving important information on the Department's mission critical assets through existence and completeness audits (Wave 3). Mission critical assets include:

- Military and General Equipment (ME and GE),
- Real Property,
- Inventory, and

- Operating Materials and Supplies (OM&S).

Ensuring that the Department's systems contain accurate and reliable information on these assets is the goal (assets recorded exist and the records are complete). As part of Wave 3, other important information will be tested and validated, such as asset condition and location. The objectives and challenges of this wave are presented in Section IV of this Report.

Just as with Wave 2, the Components have made significant progress in developing improvement plans and beginning the work for Wave 3. As shown in Figure 3, the Army's first assessable units for Military Equipment will be audit ready in the second quarter of FY 2011. Significant components of the Navy's Military Equipment (i.e., aircraft, ships, ICBMs and satellites) will be ready for an existence and completeness audit by the end of this fiscal year. The Air Force's Military Equipment will be audit ready in the first quarter of FY 2011. In addition, the Air Force will make incremental progress on important assessable units of OM&S (e.g., missile motors, cruise missiles, and drones) during FY 2011.

The Department plans to seek validation of its progress through independent examinations, starting with an examination of the Wave 1 efforts on Appropriations Received. The November 2010 FIAR Plan Status Report will more fully describe these examinations.

ACHIEVING FULL AUDITABILITY

The FY 2010 NDAA requires DoD financial statements to be validated as ready for audit not later than September 30, 2017. The Department accepts this as the current legal requirement and is committed to improving financial management with the highest priority placed on the information most often used for decision making. As discussed in this Report, the budgetary and mission critical asset priorities have been established and have enterprise-wide commitment including involvement by the Department's Chief management Officers and their Deputies.

Improving the business and financial processes in these priorities also puts the Department on the right path to achieve full auditability, because many of the processes, controls and systems that impact SBR auditability also impact full auditability. An auditable SBR requires recording obligations and outlays/expenditures accurately. These same expenditures impact the Balance Sheet as capitalized assets or the Statement of Net Cost, if expensed.

Other concurrent improvement activity, such as the deployment of the ERPs also supports achieving full auditability. The Department

intends to ensure successful ERP implementation, because they are critically needed for business operations, as well as financial improvement and auditability.

Other work required to achieve full auditability, such as determining or estimating the historical cost of existing assets, has been temporarily put on hold while the Department focuses on the SBR and existence and completeness priorities, and because this information is of limited value to DoD decision makers. Furthermore, the requirements for reporting such information may change based on the work of the CFO Council, Office of Management and Budget (OMB), and Federal Accounting Standards Advisory Board (FASAB) as they consider recommended changes to the current accounting standards and reporting requirements to improve the financial reporting framework that exists today. Under consideration are:

- Increasing the scrutiny and rigor of the most essential financial management activities and information, and
- Modifying requirements of limited value or return to Federal agencies, Congress and the taxpayer.

In addition, the USD(C) plans to ask the DoD Audit Advisory Committee to review and consider the above and to make recommendations. When the results of these efforts are complete, the Department will adjust its financial improvement plans accordingly.

CONCLUSION

The Department now has a coherent strategy and plan to progress forward on the road to improving information and achieving audit readiness for the information most often used to manage the Department. The road ahead will continue to be challenging, but with the recent changes in DoD leadership, priorities, strategy, methodology, FIAR governance (which includes the Department's Chief Management Officers), and increased resources, the Department is confident that progress will continue and will be focused to support the needs of DoD decision makers.