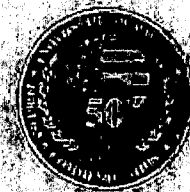




DEFENSE INTELLIGENCE AGENCY

WASHINGTON, D.C. 20340

1 October 2003



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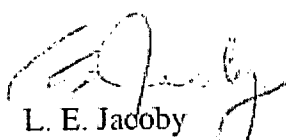
MEMORANDUM FOR THE SECRETARY OF DEFENSE

SUBJECT: Annual Statement Required Under the Federal Managers' Financial Integrity Act (FMFIA) of 1982

As Director of the Defense Intelligence Agency (DIA), I recognize the importance of management controls. I have taken the necessary steps to ensure a conscientious and thorough evaluation of management controls for DIA. The results indicate that the DIA system of internal accounting and administrative control, in effect during the fiscal year ending September 30, 2003, provides reasonable assurance, with the exception of the material weakness noted, that management controls are in place, being used, and operating effectively. Furthermore, DIA achieved the FMFIA objectives within the limits described in Tab A, which also provides information on how DIA conducted the evaluation and cites any deficiencies found in the process.

The evaluation did identify a material weakness that still requires corrective action (Tab B-1). Tab B-2 is an individual narrative on this weakness. Tab B-3 shows no material weaknesses were identified as corrected. At Tab B-4 is a summary of the significant accomplishments and actions taken to improve Component management controls during the past year.

Attachments:
As stated


L. E. Jacoby
Vice Admiral, U.S. Navy
Director

The Concept of Reasonable Assurance And How the Evaluation Was Conducted

1. The system of internal accounting and administrative control of the Defense Intelligence Agency (DIA) in effect during the fiscal year ending 30 September 2003, was evaluated in accordance with the guidance provided by Office of Management and Budget Circular (OMB) A-123 (Revised), Management Accountability and Control, 21 June 1995, as implemented by DoD Directive 5010.38, Management Control Program, 26 August 1996 and DoD Instruction 5010.40, Management Control Program Procedures, 28 August 1996. The OMB guidelines were issued by the Director of the Office of Management and Budget, in consultation with the Comptroller General, as required by the Federal Managers' Financial Integrity Act of 1982. Included is an evaluation of whether the system of internal accounting and administrative control of the DIA is in compliance with standards prescribed by the Comptroller General.

2. The objectives of the system of internal accounting and administrative control of the DIA are to provide reasonable assurance that:

- a. Obligations and costs are in compliance with applicable law.
- b. Funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation.
- c. Revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the assets.

3. The evaluation of management controls extends to every responsibility and activity undertaken by DIA and is applicable to financial, administrative, and operational controls. Furthermore, the concept of reasonable assurance recognizes that (1) the cost of management control should not exceed the benefits expected to be derived and (2) the benefits consist of reductions in the risks of failing to achieve the stated objectives. The expected benefits and related costs of control procedures should be addressed using estimates and managerial judgment. Moreover, errors or irregularities may occur and not be detected because of inherent limitations in any system of internal accounting and administrative control, including those limitations resulting from resource constraints, Congressional restrictions, and other factors. Finally, projection of any evaluation of the system to future periods is subject to risk that procedures may be inadequate because of changes in conditions, or that the degree of compliance with procedures may deteriorate. Therefore, statements of reasonable assurance are provided within the limits of the preceding paragraph.

4. The evaluation was performed in accordance with the guidelines identified above. The results indicate that the system of internal accounting and administrative control of the DIA in effect during the fiscal year that ended 30 September 2003, taken as a whole, complies with the requirement to provide reasonable assurance that the above mentioned objectives were achieved with the exception of financial management systems and processes. This position on reasonable assurance is within the limits described in the preceding paragraph.

5. DIA is divided into assessable units along organizational lines reflecting the major components of the Agency. This assessable unit structure is reflected in the DIA annual Management Control Plan. DIA will evaluate the assessable unit structure along functional lines in FY04.

6. In addition, the General Account Office (GAO) has issued its "Standards for Internal Control in the Federal Government" (GAO/AIMD-00-21.3.1, November 1999). Those standards identify the overall framework for establishing and maintaining internal control and for identifying and addressing major performance challenges and areas of greatest risk for fraud, waste, abuse and mismanagement. The GAO also has issued an "Internal Control Management Evaluation Tool" (GAO-01-1008G, August 2001) to assist agencies in maintaining or implementing effective internal control. DIA used this tool in performing our self-assessment.

Office of the Secretary of Defense (OSD) Systemic Weakness Disclosure:

DoD Directive 5010.38 requires that OSD Principal Staff Assistants (PSAs) identify and report "systemic weaknesses" that fall within their area of functional responsibility. Systemic weaknesses are management control problems identified by more than one DoD Component that are judged to be of such consequence as to potentially jeopardize the Department's operations or result in significant incidences of fraud, waste, abuse or other violations of the public trust. OSD Principal Staff Assistants (PSAs) forwarded narratives identifying OSD systemic weaknesses. Those systemic weaknesses applicable to DIA are addressed below.

Defense Intelligence Agency Financial Management Systems and Processes

Like the Department of Defense, the Defense Intelligence Agency (DIA) financial management systems and business processes do not provide accurate, reliable and timely information, thus hindering effective management decision-making. The current financial environment is comprised of many discrete systems characterized by poor integration and minimal data standardization. This absence of an overarching approach to financial management is a major obstacle preventing DIA from passing financial audits and makes this a material weakness.

Impact:

DoD continued, an inferior financial management information infrastructure hinders the efficiency and effectiveness of DIA's operations and prevents managers from making more timely and cost-effective decisions. The substandard financial management processes and information infrastructure, and the previous absence of an agency-wide, integrated approach to financial management, also contributed to the following difficulties:

- Overly complex data requirements that are driven by appropriation funding rules, elaborate policies and procedures, and outdated guidelines for excessively detailed tracking of expenditures.
- Convoluted business processes that fail to streamline excessive process steps that are further complicated by aged and disparate systems (accounting, financial and nonfinancial ("feeder")).
- Inability to meet evolving federal financial management standards.
- Difficulty in obtaining financially based, outcome-oriented, metrics for
- Decision makers. Many of the metrics currently in use reflect weak links between annual performance goals and outputs.
- Inability to produce annual financial statements that result in an unqualified audit opinion.
- Personnel who lack the technical skills necessary to support and maintain integrated financial management systems and operations.

Management Response:

DIA is improving its financial management processes, systems, and information by engaging in a number of wide-ranging initiatives:

DIA developed and briefed to OMB a plan to improve our financial management, systems, information. This plan is to help implement the President's Management Agenda goals of Improved Financial Performance and Budget and Performance Integration. At the end of the fourth quarter in 2003, DIA has accomplished more than planned.

DIA is participating in the SecDef's recently established Financial Management Modernization Program to direct and oversee financial management reform within the Department. DIA has representatives in the Accounting and Strategic Planning and Budgeting Domains. DIA hosted the DoD members of the Intelligence Community in a Classified Line of Accounting meeting, as part of this initiative. DIA continues supporting this DoD-wide management approach to improving business processes and implementing integrated financial management systems.

- DIA is also participating in National Security Agency (NSA) Working Groups, as part of NSA's efforts to develop the Intelligence Financial Management Enterprise System Pilot

for DoD. DIA is improving its own processes and legacy systems to improve the timeliness, accuracy, and relevancy of its financial management information and to aid in transitioning to the NSA and/or DoD enterprise architecture. Significant accomplishments within the last 30 days include standardization and future availability of integrated programming, budgeting and execution data. DIA is dependent on NSA's successful implementation of a new accounting system.

- DIA recently began obtaining outside advice from other federal agencies and professional audit firms to determine the necessary action to receive a "clean" opinion on audited financial statements.
- DIA is obtaining the consulting services of a professional audit firm to help develop a road map to implement all standards required for a "clean" financial opinion at the earliest opportunity.
- DIA is firmly committed to resolving auditor-identified and Federal Managers Financial Integrity Act of 1982 material weaknesses in internal controls.
- DIA has already implemented internal control recommendations contained in a June 2003 DIA Inspector General (IG) report on the Internal Control Management Program.
- DIA has already begun implementing the internal controls for improving fund distribution and reducing potential erroneous payments contained in the April 2003 Department of Defense (DoD) Inspector General (IG) Report.
- DIA established a new division (FE-4) to develop, track, and report monthly financial and performance information for routine use during operational evaluation and decision-making.
- DIA has developed financial performance metrics and General Defense Intelligence Program (GDIP) performance metrics and plan to make them available on line for the DIA Director, Chief Financial Executive (CFE), senior managers, and program and budget analysts. Included in this effort is contractor support to automate the collection of daily financial performance metrics and make it available on line.

Planned Actions:

- Complete a DIA Chief Financial Officers Strategic Plan to develop and begin implementing a complete road map for DIA enterprise architecture with integrated systems, improved processes, and standardized data, in order to obtain accurate, reliable and timely information supporting effective management decision-making and passing financial audits.
- Continue participating at Planning and Budgeting Domain Working Groups as part of the Office of the Secretary of Defense, Comptroller's Financial Management Enterprise Architecture.
- Continue participating at NSA workshops for developing a replacement of existing budget and accounting systems and an enterprise architecture.
- Continue developing an interface between NSA's financial system and DIA's

programming and budgeting systems.

- Conduct second quarterly in-process-review (IPR) of DIA financial system enhancements. Include a review of the contractor's financial statement road map.
- Review implementation of interface for two of DIA's manpower systems. Begin developing an interface for the third manpower system.
- Begin Phase 1 of a three phased implementation of the interface for DIA's financial systems.
- Begin implementing the independent audit contractor report containing a detailed and comprehensive road map of the work required to obtain a "clean" opinion on DIA's financial statements.
- Review standardized DIA line of accounting and begin development of an interface to eliminate double data entries.
- Continued bi-weekly meetings with DIA managers to implement an integrated DIA financial statement enterprise architecture.
- Continue to reengineer DIA's financially related business processes to ensure routine availability of reliable, accurate and timely financial management information.
- Begin using automated financial performance metrics and make available on line at DIA for Director to CFE to senior managers to budget analysts.
- Begin automating financial *and non-financial* performance metrics and plan to make available on line at DIA for Director to CFE to senior managers to budget analysts for monthly reporting.
- Develop a capital investment strategy and investment plan that includes costs, people, policies, processes and systems for the Department's transition to a fully integrated financial management system that is compliant with applicable federal and DoD standards.

