



DEFENSE INTELLIGENCE AGENCY

WASHINGTON, D.C. 20340-5100

INFO MEMO



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FOR: SECRETARY OF DEFENSE

THRU: UNDER SECRETARY OF DEFENSE FOR INTELLIGENCE *SL* AUG 24 2005

FROM: *L. E. Jacoby* Vice Admiral, USN, Director, Defense Intelligence Agency

SUBJECT: Annual Statement Required for FY05 under FMFIA of 1982

- I have taken the necessary steps to ensure a conscientious and thorough evaluation of the internal control program for DIA. I can provide reasonable assurance that DIA's internal controls, other than those for financial reporting, when considered as a whole, were in place, operated effectively and were being used during the fiscal year ending 30 September 2005. Our controls provide reasonable assurance that we achieved the Federal Managers' Financial Integrity Act (FMFIA) objectives of ensuring effective and efficient operations and complying with applicable laws and regulations. Details of our evaluation process are provided in TAB A.
- The evaluation confirmed that we have not yet achieved the FMFIA objective of reliable financial reporting. Unreliable financial reporting results from our dependence on outdated DoD systems and from our inability to fully support the data we input to those systems. We have identified two material weaknesses: unreliable financial systems and the inability to reconcile Fund Balance with Treasury. These weaknesses are disclosed in TAB B. We have identified unreliable financial systems as a weakness since FY03.
- Our evaluation supports my belief that the dedicated professionals of DIA use strong internal controls to enhance mission achievement. TAB B provides some examples of where we have strengthened our existing controls. Our progress in fusing controls into efficiently and effectively managing resources, achieving objectives and discouraging fraud, waste and abuse, further hones our ability to discover information and create knowledge.
- Seven reportable conditions have been disclosed in TAB C. While reportable conditions do not require reporting outside the agency, those conditions have been identified, corrective action plans developed and a monitoring system put in place to illustrate our commitment to an aggressive program that goes beyond simply meeting requirements.

Attachments: a/s

Prepared by Mr. Ken Murphy, (703) 695-5109

TAB A

THE EVALUATION

Evaluation Criteria. The Defense Intelligence Agency's (DIA) senior management evaluated the system of internal controls in effect during the fiscal year (FY) ending 30 September 2005. The evaluation was done in accordance with the Federal Managers' Financial Integrity Act (FMFIA) of 1982. The Office of Management and Budget (OMB) provides FMFIA guidance in OMB Circular No. A-123, "Management Accountability and Control," 21 June 1995. The Government Accountability Office (GAO) provides standards for FMFIA in "Standards for Internal Control in the Federal Government" and "Internal Control Management and Evaluation Tool." The Department of Defense (DoD) provides FMFIA guidance in DoD Directive 5010.38, "Management Control Program," 26 August 1996, and, DoD Instruction 5010.40, "Management Control Program Procedures," 28 August 1996.

Evaluation Objective. DIA's objective was to determine whether internal controls were in place and working to provide reasonable assurance that:

- Obligations and costs comply with applicable laws
- Funds, property, and other assets are safeguarded against waste, loss, unauthorized use, or misappropriation
- Revenues and expenditures are properly recorded, accounted for, and reported in a manner that maintains accountability over assets.

Evaluation Coverage. DIA's evaluation covered 99% of assigned personnel and resources and included sixteen major two letter (Deputy Directorates and Special Offices) organizations. Further, in 2005, some two letter organizations tasked subordinate components to submit separate statements of assurance (SOAs) to support the two letter organizational SOAs.

Evaluation Limitations. DIA's evaluation had a limited goal and process. The goal is limited to achieving a reasonable expectation that the opinion expressed about the condition of internal controls reflects the actual state of the controls. The process components for attaining a reasonable assurance also cause limitations - from the evaluator and the testing, the characteristics of fraud, and, the nature and costs of controls.

The evaluator must be qualified in the area being evaluated, and must have adequate time and resources to exercise professional care in performing the evaluation and assessing the results. The results require gathering evidence - which involves professional judgment of the areas tested; the nature, timing, and extent of the tests performed; the interpretation of test results; and the selection of appropriate controls to mitigate problems anticipated in a future time.

Fraud itself is characterized by concealment and falsification. Concealment may prevent a properly planned and performed evaluation from accurately determining and reporting the true state of affairs.

Internal controls have inherent limitations. They only address currently recognized problems, involve the allocation of resources which may not be adequate to fully implement controls, may run counter to the direction provided by Congress, and may be limited by the benefits expected.

As a result of so many limitations, qualifications, and uses of judgment, our evaluation focuses on persuading rather than convincing. Thus, this statement of reasonable assurance is a limited statement expressing a sensible opinion on an anticipated state of affairs.

Evaluation Methodology. Each of sixteen DIA organizations provided an organizational SOA certified by the organizational head.

Each organization was provided DIA's automated self assessment tool derived from GAO's "Standards for Internal Control in the Federal Government," and "Internal Control Management and Evaluation Tool." The tool was initially developed and fielded in 2003. It was revised with each use in 2004 and in 2005. The tool now contains 154 questions segmented into the five GAO standards. Each segment leads to an overall deductive conclusion on the five standard areas of control environment, risk assessment, control activities, information and communication, and monitoring. The tool also provides a preliminary assessment of the 2006 area of financial reporting. Use of the tool facilitates an inductive conclusion on the general risks faced and on the state of internal controls within each organization.

Organizations are required to supplement the self assessment tool with other sources of information to support their overall assessment conclusion. Other sources of information include recognition and documentation of Internal Control Program (ICP) accomplishments. The most significant improvements made during the past year are detailed in Tab B, "ICP and Related Accomplishments." Other sources include the results of internal and external reviews. These are discussed and detailed in CORROBORATING INDICATORS section of Tab A. The organizational assessment is conducted by an ICP coordinator appointed by the organization head and trained and assisted by the DIA ICP Office.

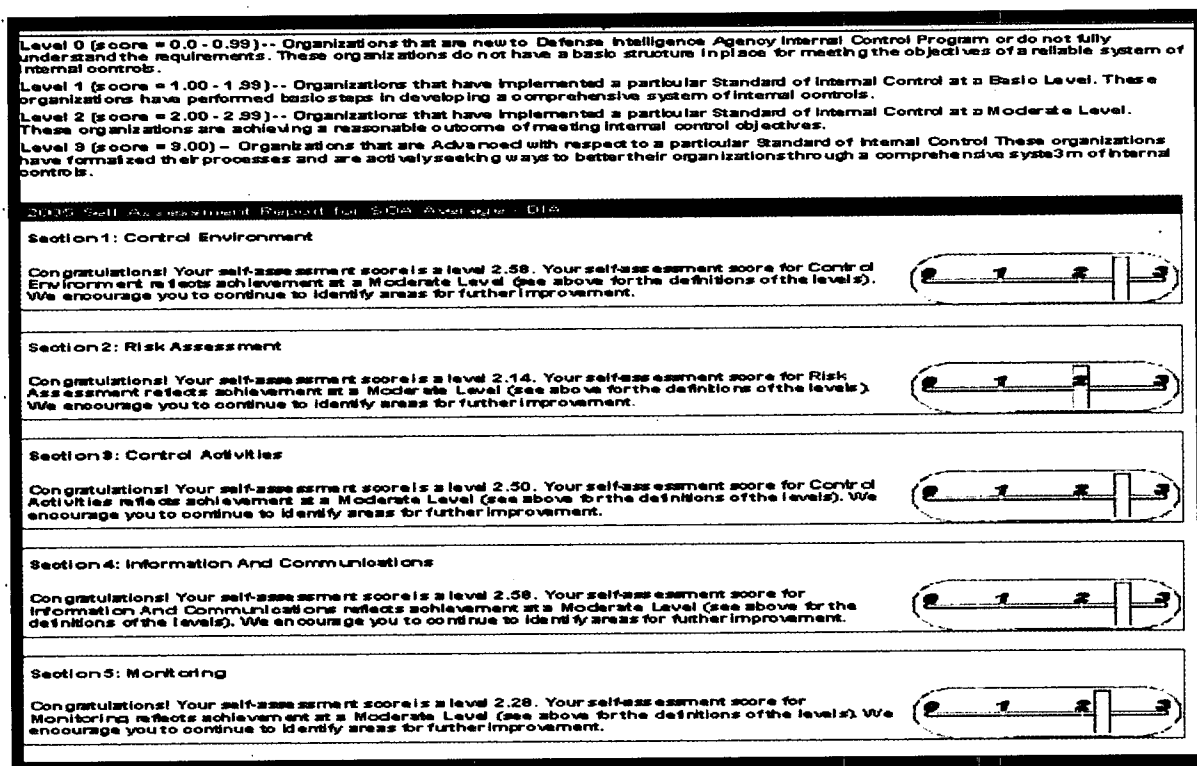
Evaluation Conclusion. This evaluation, performed within described limitations, resulted in a qualified SOA.

The results indicate that DIA's system of internal controls, excepting those in financial reporting, when considered as a whole, were in place, operated effectively, and were being used during the fiscal year (FY) ending 30 September 2005. The results provide a basis for reasonable assurance that DIA achieved the FMFIA objectives of ensuring effective and efficient operations and complying with applicable laws and regulations.

The evaluation confirms that we have not yet achieved the FMFIA objective of reliable financial reporting. Unreliable financial reporting results from our dependence on outdated DoD systems, and from our inability to support fully the data we inputs to those systems. As a result, we have

identified two material weaknesses: unreliable financial systems and the inability to reconcile Fund Balance with Treasury and disclosed these in Tab B. Unreliable financial systems were first identified as a material weakness in FY 2003 and we reported it each subsequent year. Inability to reconcile Fund Balance with Treasury is now identified as a material weakness and disclosed in Tab B. Seven reportable conditions related to data input have been identified in our supplemental Tab C. While reportable conditions do not require reporting outside the Agency, those conditions have been identified, corrective action plans developed and a monitoring system put in place to illustrate our commitment to an aggressive program that goes beyond simply meeting requirements. Adding a supplemental Tab C to track and manage reportable conditions illustrates our commitment to an aggressive program that goes beyond simply meeting requirements.

The self-assessment tool scoring indicated that the Agency had achieved a moderate (intermediate) level of scoring on implementation of GAO's five internal control standards. The 2005 Agency-wide averages improved for all the sections that were also assessed in 2004. Specifically, control environment improved 3.6 percent, control activities improved 9.7 percent, and risk assessment improved 18.2 percent. Risk assessment was at the low (basic) level in 2004 and improved significantly by achieving the moderate level. The tool generates a graphic that visually shows scoring in each area. The graphic below shows the Agency's overall scoring that resulted from consolidating the organizational submissions.



TAB A

CORROBORATING CONSIDERATIONS

Internal Reviews

Office of the Inspector General. The Office of the Inspector General (OIG) provided 40 documents from their 2005 audits, reviews, evaluations, investigations, inspections, and assessments. Three specifically referred to weaknesses in internal controls.

1. "Logistics Business Evaluation" (Project Number 04-2135-HQ-003; 23 November 2004) stated: "The current condition of Agency property accountability, and the inability of financial, acquisition, and logistics systems to cohesively and accurately integrate data, reflects a substantial internal control weakness for accountability and control of DIA capital assets." The inability of financial, acquisition, and logistics systems to integrate data is disclosed as a material weakness in Tab B. The condition of property accountability is disclosed as a Reportable Condition in Tab C.

2. "ISG (Iraq Survey Group) Property Accountability" (Project Number 05-2548-OA-031, 8 June 2005) stated: "The lack of an effective internal control structure resulted in inaccurate property records, staffing and mission support deficiencies, and inadequate documentation to accurately record obligations in DIA accounting records." The condition of property accountability is disclosed as a reportable condition in Tab C. The condition of inaccurate obligation documentation is disclosed as a reportable condition in Tab C.

3. "CT (Counterterrorism) Contracting Audit" (Project Number 03-2168-OA-023, 31 January 2005) stated: "The lack of a single source of readily available, comprehensive, reliable acquisition vehicle information indicates an internal control weakness which may adversely impact AE-2's (Acquisition Executive) ability to provide timely, accurate information necessary for management reporting and decision-making." Management comments to the recommendation stated that the information is available from multiple sources but the single source condition will be addressed with the implementation of an end-to-end life cycle acquisition management system. The OIG stated that these comments were responsive. This is not disclosed as a reportable condition.

OIG Challenges Identified for Performance and Accountability Report. The OIG provided a summary of the management and performance challenges that were identified in their work for inclusion into the Agency's fiscal year (FY) 2005 Performance and Accountability Report (PAR). There were five challenges identified:

1. Property Accountability. "The area of property accountability continues to present a challenge as corrective actions are planned and implemented. An OIG Logistics Evaluation identified the current condition of Agency property accountability – coupled with the inability of financial acquisition and logistics system to cohesively and accurately integrate data – as an

internal control deficiency for accountability and control of Agency assets.” This condition is disclosed as a reportable condition in Tab C.

2. **Fiscal Management/Reporting.** A draft auditability assessment report “identified a number of management and performance challenges to include: the accuracy of – and supporting documentation for – the recorded amounts for plant, property, and equipment; lack of a standard periodic process for reconciling accounting detail with subsidiary detail, and DIA’s reliance on the National Security Agency (NSA) to provide the accounting/general ledger system that serves as DIA’s system of record.” The property accountability condition is disclosed as a reportable condition in Tab C. Lack of reconciliation is disclosed as part of the new Material Weakness disclosed in Tab B. Reliance on the nonintegrated NSA system is part of the material weakness disclosed in Tab B.

3. **Data Linkage.** “OIG identified recurring issues with the inability of decision-makers to reconcile information among separate information technology support systems. For example, during the conduct of the logistics business evaluation, OIG found that the ability of DIA to manage property accountability was inhibited by limitations on linkages among the financial, acquisition, and logistics information system. The team conducting the assessment of the ISG found similar issues in the ability to link financial and property information necessary to reconcile financial data.” The lack of integration of financial systems is disclosed as a material weakness in Tab B.

4. **Collection Management Program Communication.** There were a lack of current operating directives from headquarters to drive field collection and a limited number of evaluations provided to the field on their intelligence information reports. Improvements in the currency of operating directives were observed during more recent inspections. The OIG indicated that this was not considered a significant weakness, and this item is not disclosed as a reportable weakness.

5. **Information Technology Support to the Field.** Inspection teams found that field activities did not have a common suite of information technology (IT) support tools. A new IT support program has been tested and will be deployed. Since this issue will be resolved with deployment of the new support program, this item is not disclosed as a reportable weakness.

Office of the Inspector General Three Year Trend Analysis. The OIG reviewed the inspections, evaluations, and assessments that the inspections unit had completed since the beginning of FY 2003. The purpose was to identify common trends in OIG findings and recommendations that might further enable continuing performance improvements consistent with the Director’s Strategic Intent and the specific tasks from the Agency Mission Essential Task List. The review included more than 80 separate field activities and 18 organizational, functional, or process issues under headquarters purview.

The review noted that OIG recommendations in the reports had been, or were being, acted upon. This observation addressed the GAO internal control monitoring standard that requires audit findings be promptly resolved. The review highlighted the contribution that a strong metrics-driven internal management control program can make to inform management decision-making

and improve organizational performance. The review also noted that Defense Attaché Offices and field operation units were held in the highest regard by the embassy country teams and combatant command personnel supported which served as a testament to, and measure of, mission success. The review did not specifically identify any material weaknesses.

External Reviews

There were not any GAO or DoD IG reports provided which included the DIA during FY 2005.

TAB A

SYSTEMIC WEAKNESSES

LISTING OF DOD SYSTEMIC WEAKNESSES AND RELATED DIA WEAKNESSES

1. Financial Management Systems and Processes.

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|--|--------------------|
| a. Material Weakness - Reconciling Fund Balance With Treasury. | Tab B-2, Page B-2. |
| b. Material Weakness - Unreliable Financial Management
Systems and Processes. | Tab B-2, Page B-4. |
| c. Reportable Condition - Lack of Established Financial Policies. | Tab C, Page C-2. |
| d. Reportable Condition - Lack of Documented Business Processes. | Tab C, Page C-4. |
| e. Reportable Condition - Lack of Implementing Procedures. | Tab C, Page C-6. |
| f. Reportable Condition - Monitoring Unliquidated Obligations. | Tab C, Page C-8. |
| g. Reportable Condition - Reliability of Financial Information. | Tab C, Page C-10. |

2. Management of Information Technology and Assurance.

3. Environmental Liabilities.

4. Personnel Security Investigations Program.

5. Real Property Infrastructure.

6. Government Card Program Management.

7. Valuation of Property, Plant, and Equipment on Financial Reports.

- | | |
|---|-------------------|
| a. Reportable Condition - Reliability of Financial Information. | Tab C, Page C-12. |
|---|-------------------|

8. Valuation of Inventory on Financial Reports.

9. Improper Use of Non-Department of Defense Contracting Vehicles.

- | | |
|---|-------------------|
| a. Reportable Condition - Risk Assessment and Documentation
in Acquisition Management. | Tab C, Page C-15. |
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TAB A

SYSTEMIC WEAKNESSES

NARRATIVE OF DOD SYSTEMIC WEAKNESSES AND RELATED DIA WEAKNESSES

Reporting Requirement. DoD Directive 5010.38 requires the Office of the Secretary of Defense (OSD) principal staff to identify and report “systemic weaknesses” falling within their functional responsibility area. Systemic weaknesses are those which may potentially jeopardize the department’s operations or result in significant instances of fraud, waste, abuse or violation of the public trust. These weaknesses may be identified by OSD principal staff as cutting across functional responsibility areas, occurring in more than one DoD component, or, as reported by more than one DoD component. DoD components are required to list each OSD identified systemic weakness and identify whether their component shares the weakness.

1. DoD Financial Management Systems and Processes. “DoD financial and business management systems and processes are costly to maintain and operate, not fully integrated, and do not provide information that is reliable, timely, and accurate. The estimated correction date is 4th Quarter FY 2007.”

In 2003, DIA identified the absence of an overarching approach to financial management as a material weakness preventing DIA from passing financial audits and obtaining a “clean” audit opinion. This material weakness remains and is disclosed in Tab B. A new weakness related to reconciling Fund Balance with Treasury also is disclosed in Tab B. Related financial management systems, processes, policies, procedures, and data input weaknesses are disclosed as reportable conditions in Tab C.

2. Management of Information Technology and Assurance. “DoD information systems are potentially vulnerable to an information warfare attack. In addition, this issue has also been reported as a “significant deficiency” under the reporting requirements of the Federal Information Security Management Act. The estimated correction date is 3rd Quarter, FY 2007.”

The DIA Chief Information Officer has not declared this to be a DIA material weakness. This decision was based on the many improvement initiatives, some detailed in Tab B, “ICP and Related Accomplishments.” A weakness was identified in the July 2004 DIA OIG Federal Information Security Management Act (FISMA) independent evaluation (Project 04-2320-OA-006) and was reported as a Management Control Weakness (Reportable Condition) in the Fiscal Year 2004 Statement of Assurance. This reportable condition was reported as corrected in a FY 2005 FISMA Quarterly Update and is not disclosed in our supplemental Tab C.

3. Environmental Liabilities. “The DoD has not developed the policies, procedures and methodologies needed to ensure that cleanup costs for all of its ongoing and inactive or closed

operations are identified, consistently estimated, and appropriately reported. Site inventories and cost methodologies to identify budget requirements and financial liabilities continue to need improvement. The estimated correction date is 1st Quarter FY 2006.”

This weakness does not apply to DIA. Policies for Environmental Liabilities have been developed. At the location with the most potential for liabilities, there is an inter-service support agreement which transfers environmental issue responsibility to the host installation.

4. Personnel Security Investigations Program. “DoD hiring is adversely affected because personnel security investigations are backlogged. The estimated correction date is 4th Quarter FY 2006.”

This issue does impact DIA, but management did not declare this as a material weakness. This decision was based in part on management’s analysis of outstanding cases. In June 2004, there were 5,000 pending cases with 2,700 older than 360 days. In June 2005, there are 4,000 pending cases with 780 older than 360 days. This is a significant improvement some of which is the result of the use of DIA’s contract Background Investigations Provider and the assignment of eight contractors to the Central Clearance Branch.

5. Real Property Infrastructure. “The Department has not adequately managed the real property infrastructure to halt the deterioration or obsolescence of facilities on military installations. The estimated correction date is 1st Quarter FY 2008.”

This weakness does not apply to DIA. In FY 2003, DIA identified the need to enhance facility operations, maintenance, and repair activity. The Agency used the Regional Base Operations and Support Services contract to acquire a maintenance workforce. The contract includes a proactive preventive maintenance program. Under the program, the Agency invested millions of dollars in recapitalizing the support infrastructure and renovating DIA facilities on Bolling Air Force base. The program’s schedule runs through 2012, and will recapitalize the support infrastructure and renovate office environments with state of the art technology.

6. Government Card Program Management. “Instances of misuse, abuse, and fraud in respect to purchase and travel card use, and centrally billed accounts, have been attributed to inadequate DoD emphasis on proper use of the cards, poorly enforced controls, and lax oversight. The estimated correction date is 4th Quarter FY 2006.”

For travel charge cards, DIA’s area of concern was misuse and late payment. DIA’s performance has been continuously improving. DoD’s Performance Indicator Goal for this area is 1.5 percent for past due accounts. DIA exceeded this goal with past due accounts representing only 0.9 percent of open Agency accounts. Further, inappropriate use of travel cards is documented and corrected. Suspicious activity is referred to supervisors, Counterintelligence and Security Activity, and the IG for further review and disciplinary action, if appropriate.

For purchase cards, DIA’s primary area of concern was refresher training. DIA’s Office of Engineering and Services is collaborating with the DoD Program Office to develop a compact

disc version for the training. The compact disc will provide users worldwide the ability to complete the training anytime even when online access is unavailable.

7. Valuation of Property, Plant, and Equipment on Financial Reports. “The DoD is unable to accurately report the value of property, plant, and equipment on its financial statements. The estimated correction date is 4th Quarter FY 2006.”

This DoD weakness does apply to DIA; however, management has chosen to disclose it as a reportable condition in our supplemental Tab C.

8. Valuation of Inventory on Financial Reports. “The valuation of inventory is not always correctly reported. The estimated correction date is 2nd Quarter FY 2006.”

This weakness does not apply to DIA. The Agency does not own stocks for resale; therefore, the inventory weakness does not apply to DIA.

9. Improper Use of Non-Department of Defense Contracting Vehicles. “Non-Department of Defense contracting vehicles have been used improperly to procure services or supplies. The estimated correction date is 2nd Quarter, FY 2006.”

This weakness is not known to apply to DIA. However, to validate this conclusion, the area is being included as part of the contract risk assessment being performed in the AE. The lack of an overall risk assessment is disclosed as a reportable condition in our supplemental Tab C.

TAB B-1

LISTING OF UNCORRECTED AND CORRECTED MATERIAL WEAKNESSES

Uncorrected Weaknesses Identified During the Period

Title: Reconciling Fund Balance with Treasury
Category: Comptroller and/or Resource Management
Targeted Correction Date: 4th Quarter 2007
Page Number: Tab B-2, Page B-2

Uncorrected Weaknesses Identified During Prior Periods

Title: Unreliable Financial Management Systems and Processes
Category: Comptroller and/or Resource Management
Year First Report: FY 2003
Correction Quarter and Fiscal Year Date:
Per Last Annual Statement 4th Quarter 2006
Per This Annual Statement 4th Quarter 2007
Page Number: Tab B-2, page B-4

Corrected Weaknesses Identified During All Periods

Title: None
Year First Report: Not Applicable
Page Number: Not Applicable

TAB B-2

NARRATIVE FOR UNCORRECTED MATERIAL WEAKNESS IDENTIFIED DURING THE PERIOD

Reconciling Fund Balance with Treasury

Description of the Issue: There is no effective process for ensuring that financial transactions (i.e., disbursements and collections) executed by service providers (i.e., Defense Finance and Accounting Service (DFAS) and the National Security Agency (NSA)) impacting Fund Balance with Treasury (FBWT) are properly recorded in DIA's accounting system. This situation makes the overall amount reported as FBWT on DIA's financial statements unreliable. FBWT represents the majority of assets on DIA's balance sheet and the account has never been reconciled.

Functional Category: Comptroller/Resource Management

Pace of Corrective Action:

Year Identified: 2005
Original Targeted Correction Date: 4th Quarter 2007
Targeted Date in Last Report: N/A
Current Targeted Correction Date: 4th Quarter 2007

Reason for Change in Dates: First time reported.

Appropriation:

<u>Title</u>	<u>Appropriation</u>	<u>FY2005</u>	<u>FY2006</u>	<u>FY2007</u>	<u>Total</u>
O&M	97x0100	\$0.2M	\$1.4M	\$1.0M	\$2.6 M

Validation Indicators: Final indicator will be a successful audit of the balance sheet with an opinion being rendered on the FBWT amount on the statement. Interim progress is shown in annual Department of Defense Inspector General (DoD IG) financial statement reviews requested by the Senate Select Committee on Intelligence (SSCI). The reviews are supplemented by the SSCI requested "Annual Report on IC (Intelligence Community) Compliance with Federal Accounting Standards." Quarterly, the CFE (Chief Financial Executive) reports on improving financial performance for the President's Management Agenda scorecard. Monthly, the CFE provides progress updates to the Office of the Secretary of Defense (Comptroller) (OSD (C)) Mid-Range Financial Improvement Plan.

Results Indicator: The key results will be reliable, auditable financial statements. As each financial statement becomes ready for audit, an assertion package will be prepared. In the

interim, assessments by certified public accounting firms help provide progress on achieving auditable financial statements.

Source Documents: The following sources identified this issue:

1. Urbach Kahn and Werlin LLP, Certified Public Accountants, prepared an "Auditability Assessment Report" under contract with DoD IG.
2. DoD IG prior reports on the Reliability of DIA Financial Statements and Processes (Report Number D-2004-079, 29 April 2004; Report Number 2003-74, 7 April 2003; Report Number D-2002-117, 25 June 2002)
3. DoD FY 2004 Performance and Accountability Report (PAR), Compliance With Legal and Regulatory Requirements, "Chief Financial Officers Act." The DoD 2004 PAR cites this as an auditor identified financial statement material weakness. The weakness applies to DIA because DIA relies on the same systems.

Progress to Date:

1. Established a Chief Financial Officers (CFO) Act Compliance Senior Leader position and staffed.
2. Established a Financial Statements Office and staffed.
3. Tasked KPMG certified public accountant contractors to assist in CFO Act compliance.
4. Established FBWT as specific balance sheet task with planning and execution schedule.

Major Milestones:

1. Milestones for FY 2006: Establish baseline for reconciliation: 4th Quarter FY 2006.
2. Milestones beyond FY 2006: Reconcile cash with Fund Balance with Treasury: 1st Quarter FY 2007.

TAB B-2

NARRATIVE FOR UNCORRECTED MATERIAL WEAKNESS IDENTIFIED DURING PRIOR PERIODS

Unreliable Financial Management Systems and Processes

Description of the Issue: 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 composed of many discrete systems characterized by poor integration and minimal data standardization. This absence of an overarching approach to financial management is a material weakness preventing DIA from passing financial audits and obtaining a “clean” audit opinion. Further, most other Department of Defense (DoD) financial management systems and business processes are not integrated and are unable to produce reliable financial reports. DIA relies on the National Security Agency system to provide accounting services.

Functional Category: Comptroller/Resource Management

Pace of Corrective Action:

Year Identified: 2003
Original Targeted Correction Date: 4th Quarter 2006
Targeted Date in Last Report: 4th Quarter 2006
Current Targeted Correction Date: 4th Quarter 2007

Reason for Change in Dates: Delay by National Security Agency (NSA) (accounting service provider) in implementing compliant financial management system until FY 2007.

Appropriation:

Title	Appropriation	FY2005	FY2006	FY2007	FY2008	Cost to Complete	Total
O&M	97x0100	\$8.0M	\$5.0M	\$4.7M	\$5.9M	\$20.5M	\$44.1M

Validation Indicator: Final indicator will be a successful financial statement audit with an opinion being rendered on the financial management system (e.g., Statement of Auditing Standards 70 review). Interim progress is shown in annual Department of Defense Inspector General (DoD IG) financial statement reviews requested by the Senate Select Committee on Intelligence (SSCI). The reviews are supplemented by the SSCI requested “Annual Report on IC Compliance with Federal Accounting Standards.” Quarterly, the Chief Financial Executive (CFE) reports on improving financial performance for the President’s Management Agenda scorecard. Monthly, the CFE provides progress updates to the Office of the Secretary of Defense (Comptroller) (OSD (C)) Mid-Range Financial Improvement Plan.

Results Indicator: The benefits will be reliable, auditable financial statements. Appendix B to the Chief Financial Officer (CFO) Act Compliance Plan provides the measures reported quarterly to the CFE. Those measures relating to integration include the percent of feeder systems interfaced to the accounting system.

Source Documents: The following sources identified this issue:

1. Urbach Kahn and Werlin LLP, Certified Public Accountants, prepared an "Auditability Assessment Report" under contract with DoD IG.
2. DoD IG prior reports on the Reliability of DIA Financial Statements and Processes (Report Number D-2004-079, 29 April 2004; Report Number 2003-74, 7 April 2003; Report Number D-2002-117, 25 June 2002).
3. DoD FY 2004 Performance and Accountability Report, Section 2, Systemic Weaknesses, "Department of Defense financial and business management systems and processes are costly to maintain and operate, not full integrated, and do not provide information that is reliable, timely, and accurate."
4. DoD FY 2004 Performance and Accountability Report, Section 4, Systemic Weaknesses, "Department of Defense systemic deficiencies in financial management systems and business processes result in the inability to collect and report financial and performance information that is accurate, reliable, and timely."

Progress to Date:

1. Established a Financial Business Systems Office and staffed with a newly established Senior Expert position and supporting staff supplemented by contractors.
2. Awarded three contracts for assisting with implementation of financial management solutions and ensuring integration of the systems.

Major Milestones:

1. Milestones for FY 2006: NSA currently projects an Initial Operating Capability (IOC) for core financials of 4th Quarter FY 2006.
2. Milestones beyond FY 2006: DIA will cutover to the FMS/FACTS system in the 1st Quarter FY 2007.

TAB B-3

NARRATIVE FOR MATERIAL WEAKNESSES CORRECTED DURING CURRENT PERIOD

There were no material weaknesses corrected in FY 2005.

However, the Information Assurance Reportable Condition reported in FY 2004 was reported as corrected during FY 2005 in the Quarterly Federal Information Security Management Act Report.

TAB B-4

INTERNAL CONTROL PROGRAM AND RELATED ACCOMPLISHMENTS

Training

Training was conducted throughout the entire organization.

Organizational Internal Control Program (ICP) coordinators are trained upon appointment and given refresher training by the Defense Intelligence Agency (DIA) ICP Office prior to beginning the annual self assessment. Organizations reporting weaknesses are provided advice and assistance by the DIA ICP Office prior to disclosing these in organizational Statement of Assurance (SOAs). Organizational ICP training includes training materials, guidance, prior statements of assurance, and templates for developing assessable units and managing organizational internal control programs.

In January 2005, the DIA board of directors was given an executive level training session on the DIA ICP. The training introduced internal controls, discussed the laws requiring them, described deputy director responsibilities in the program, highlighted the organizational ICP coordinator's role, assessed the process for 2005, and previewed the impending changes related to financial reporting that is coming in 2006.

In June 2005, the satellite resource managers were provided a special training session introducing internal controls and emphasizing the financial reporting changes coming with 2006. The Chief Financial Executive (CFE) has personnel assigned as financial advisors in each of the DIA organizations (satellites).

In July 2005, ICP training was provided to the Comptroller workforce at an all-hands meeting. The training session introduced internal controls, discussed the requirements of the Chief Financial Officer (CFO) Act, audit opinions, and emphasized the financial reporting changes coming with 2006.

In July 2005, the Joint Intelligence Virtual University (JIVU) has contracted to create interactive and engaging web-based training for managers. JIVU offers a structured, controlled environment that allows delivery of training to users' workstations via JIVU's website. Anticipated completion date for the online manager's course is December 2005. The online course will provide an overview of internal controls, a general overview of DIA's Manager's Internal Control Program requirements, Statement of Assurance process, and will provide certification online. The course will aid managers to develop and implement cost effective internal control for results-oriented management, assess and document the adequacy of internal controls in programs and operations, assess and document internal controls over financial reporting, identify needed improvements, and take corrective action.

In August 2005, the JIVU has contracted to develop web-based internal control training for all DIA employees. The course is geared toward the entire workforce especially individuals without management responsibilities and will provide certification online. The course objectives are to enable the user to define internal controls, be familiar with examples of internal controls, and understand the consequences when internal controls don't work. The DIA ICP Office developed the course objectives and content for this course. The course will be delivered through the online JIVU. Anticipated fielding of the employees' course is October 2005.

Component Wide Automated Self Assessment Tool

The DIA ICP Office further developed its automated self assessment tool. The tool was derived from GAO's "Standards for Internal Control in the Federal Government" and "Internal Control Management and Evaluation Tool." The tool was initially developed by a contractor and fielded in 2003. However, feedback from the respondents indicated that majority found many of the questions, especially those involving risk, to be incomprehensible. The questions were revised with each use in 2004 and again in 2005. The tool currently contains 154 questions segmented into the five GAO standards. Many of the questions have sub questions which help clarify and expand on the main question. Each segment leads to an overall deductive conclusion on each of the five standards areas of control environment, risk assessment, control activities, information and communication, and monitoring. The 2005 tool also provides a preliminary introduction and assessment of the new 2006 area of financial reporting. Use of the tool facilitates inductive conclusions on the general risks faced and on the general state of internal controls within each organization.

Correction of Information Assurance Reportable Condition

The FY 2004 Statement of Assurance (SOA) disclosed a "Management Control Weakness" (now referred to as a reportable condition) in the area of information assurance. The weakness involved an incomplete inventory of information technology systems and exceeding the three year re-accreditation requirements. The weakness was identified in the July 2004 DIA OIG Federal Information Security Management Act (FISMA) independent evaluation (Project 04-2320-OA-006). The weakness was reported as corrected in the Quarterly FISMA FY 2005 report.

Correction of Causes for DoD IG Audit Findings

The Senate Select Committee on Intelligence requested intelligence agencies to annually report on the reliability of their financial statements. The Department of Defense Inspector General (DoD IG) reviewed DIA's financial management and reported numerous control weaknesses and deficiencies. The primary causes cited were deficient accounting systems, improper procedures, and inadequate staff. To address the accounting systems issue, DIA established a senior leader position, staffed the Business Systems Office, and engaged substantial contract support. To address the procedures issue, DIA established and staffed the Comptroller's Policy Office, the Comptroller's Internal Control Office, and engaged significant contract support. The staffing issue was further addressed by establishing and staffing the Comptroller and CFO Act

Compliance senior leader positions, establishing and staffing a Comptroller's Financial Statement Office, and by contracting further support including funding a Certified Public Accounting firm auditability assessment.

Component Wide Performance Expectations

The Directorate for Measures and Signatures Intelligence and Technical Collection (DT) became the first organization to fully implement the CFE's FY 2005 memorandum to revise performance expectations of all personnel whose responsibilities include significant internal control responsibilities. DT revised performance expectations of all personnel whose responsibilities included property accountability or fund certification to have internal controls responsibilities included in their performance expectations.

Information Assurance Tool

DIA has deployed a network and vulnerability scanning tool. The tool discovers network devices, assets, and unauthorized applications (such as P2P, malware, or spyware); performs audits for known vulnerability and configuration issues; and recommends and prioritizes remediation actions to address the identified vulnerabilities. Complete network vulnerability scans are programmed for FY 2006.

Information Assurance Awareness Training

Eighty one percent of the DIA workforce has received information technology security awareness training. This is accomplished through the use of computer-based training that is accessible via the Joint Intelligence Virtual University. In addition, all new employees are given an information assurance (IA) awareness briefing as part of their mandatory in processing course.

Information Assurance Enterprise Risk Management System

An Enterprise Risk Management System (ERMS) was deployed at all five Regional Service Centers. The ERMS consists of a comprehensive set of IA tools to facilitate vulnerability assessments, information assurance vulnerability-alert compliance verification and malicious code scanning. ERMS supports Certification and Accreditation vulnerability remediation, FISMA reporting, Congressional Directed Actions, and provides critical information on enterprise security posture.

Data Cleansing Lab Established

An off-site lab was created to supplement embedded personnel and resolve unliquidated obligations (ULOs). On-site personnel send documents with ULOs to the lab to be researched. The lab team researches, collaborates, and resolves ULOs. The lab team allows on site personnel to focus on resolving classified ULOs. The lab also provides training for personnel awaiting clearances so that when the clearances arrive, personnel are experienced and ready to function on site.

Data Cleansing Effort

The data cleansing effort began in March 2005 to clean the data in DIA financial systems prior to implementing a new system. The objective was to ensure that the data entering the new system was valid. Business rules, policies and procedures were developed and disseminated to the workforce. A data cleansing toolkit was created which outlines the functional processes for data cleansing, provides job aids for Mechanization of Contract Administrative Services (MOCAS) and Electronic Document Access system applications. Since March, 13,700 transactions worth \$190 million have been cleansed.

PART Performance

The Directorate for Measures and Signatures Intelligence and Technical Collection (DT) was evaluated by the Office of Management and Budget using the Program Assessment and Rating Tool (PART). PART evaluates a program's performance in four areas: purpose and design, strategic planning, program management, and program results. DT received an overall rating of 72 percent, Moderately Effective, placing DT in the top 30 percent of the programs PARTed since 2002. DT worked closely with DIA's Financial Executive group which favorably impacted the rating. DT is sharing its PART experience with other DIA directorates to help them prepare for their own PART experience.

Radio Frequency Identification Tags

A Radio Frequency Identification (RFID) system was implemented to assist with property inventories. This new technology incorporates a small tag permanently attached to each piece of equipment using ultraviolet light and a radio receiver that picks up the signal from the tag. Each tag uniquely identifies each piece of equipment. During an inventory check, the radio receiver is pointed at the equipment and the identifier is automatically recorded. The information is recorded on a disk and then transferred to the Property Accountability Support System. This innovation is at the leading edge of logistics management as the Department of Defense will not have this system for several years.

Combat Contracting Officer's Technical Representative

The deployment of the Iraq Survey Group (ISG) was the largest intelligence mission in the DIA's history and involved hundreds of military and civilian personnel and thousands of contractors. Concerned with oversight of contractors who comprised about 80 percent of the ISG, the Chief Acquisition Executive created the Combat Contracting Officer's Technical Representative unit. The unit received special training and was deployed in direct support of the ISG and the DIA. The new unit is an innovative way of achieving accountability of forward contracting operations and ensuring performance management of contractors on the battlefield.

DIA IG Trend Analysis

The Office of the Inspector General (OIG) reviewed inspection, evaluations, and assessments the inspections unit completed since the beginning of fiscal year (FY) 2003 to identify common trends in OIG findings and recommendations that might further enable continuing performance improvements. The reports assessed more than 80 separate field activities and 18 organizational, functional, or process issues under the headquarters element purview. Advisory suggestions for management actions were made. The OIG analysis highlighted the contribution that a strong metrics-driven internal management control program can make in informing management decision-making and improving organizational performance.

Appropriation Law Training

The Financial Executive has increased the level of workforce personnel taking the appropriations law training from 30% to 44% during FY 2005.

Defense Acquisition Workforce Improvement Act Manager

The Acquisition Executive (AE) established a position to oversee and manage the requirements of the Defense Acquisition Workforce Improvement Act (DAWIA). AE hired a DAWIA manager to ensure contract specialists, contract officers, and other DIA acquisition workforce members get certified at their proper levels and meet their continuing education requirements.

Acquisition Executive Satellite Support

AE reorganized its offices out of the traditional "production pool" environment to one around the customer, very similar to the Financial Executive Satellite concept. This was done to leverage forward deployed staff and other staff now embedded physically within key customer organizations and sites to facilitate early acquisition planning and the team approach to acquisition.

Contracting Officer Representative Guidance

A comprehensive Contracting Officer Representative (COR) Deskbook was made available in both hard and soft copy. Additionally, on-site COR training courses were conducted. Over 180 CORs were trained in FY 2005. Mandatory COR training is being transitioned from the classroom to the web to facilitate training access for the Agency's worldwide workforce.

TAB C-1

LISTING OF REPORTABLE CONDITIONS

<u>Title:</u>	Lack of Established Financial Policies.
<u>Category:</u>	Comptroller and/or Resource Management.
<u>Page Number:</u>	Tab C-2, Page C-2.
<u>Title:</u>	Lack of Documented Business Practices.
<u>Category:</u>	Comptroller and/or Resource Management.
<u>Page Number:</u>	Tab C-2, Page C-4.
<u>Title:</u>	Lack of Implementing Procedures.
<u>Category:</u>	Comptroller and/or Resource Management.
<u>Page Number:</u>	Tab C-2, Page C-6.
<u>Title:</u>	Monitoring Unliquidated Obligations.
<u>Category:</u>	Comptroller and/or Resource Management.
<u>Page Number:</u>	Tab C-2, Page C-8.
<u>Title:</u>	Reliability of Financial Information (Payables, Receivables).
<u>Category:</u>	Comptroller and/or Resource Management.
<u>Page Number:</u>	Tab C-2, Page C-10.
<u>Title:</u>	Reliability of Financial Information (Plant, Property, Equipment).
<u>Category:</u>	Supply Operations.
<u>Page Number:</u>	Tab C-2, Page C-12.
<u>Title:</u>	Risk Assessment and Documentation in Acquisition Management.
<u>Category:</u>	Acquisition.
<u>Page Number:</u>	Tab C-2, Page C-15.

TAB C - 2

REPORTABLE CONDITIONS

Lack of Established Financial Policies

Description of the Issue: Defense Intelligence Agency (DIA) does not have a formal, documented set of financial policies. Such policies are essential in order to ensure business processes are properly designed and to develop specific financial procedures. Furthermore, established policies will document DIA's adherence to meeting accounting standards (Financial Accounting Standards Advisory Board - FASAB) and in support of Federal financial legislation (e.g., Chief Financial Officers (CFO) Act and Federal Financial Management Improvement Act (FFMIA)).

Functional Category: Comptroller/Resource Management

Pace of Corrective Action:

Year Identified: 2005
Original Targeted Correction Date: 4th Quarter FY 2006
Targeted Correction Date in Last Report: First time reported
Current Target Date: 4th Quarter FY 2006

Reason for Change in Dates: No change. First time reported.

Appropriation:

<u>Title</u>	<u>Appropriation</u>	<u>FY2005</u>	<u>FY2006</u>	<u>FY2007</u>	<u>FY2008</u>	<u>Total</u>
O&M	97x0100	\$0.2M	\$1.5M	\$0.5M	\$0.3M	\$2.5M

Validation Indicator: Initial indicator will be a defined set of business rules to serve as a foundation for a set of financial policies. Final indicator will be a documented set of financial policies applicable to DIA and readily accessible by DIA staff. Additionally, these financial policies will drive the development of business processes and detailed procedures within DIA.

Results Indicator: Documentation of DIA's accounting control activities in support of the new Office of Management and Budget (OMB) Circular A-123 requirements will show progress in the development of financial policies.

Source Documents: The following sources identified this issue:

1. Urbach Kahn and Werlin LLP, Certified Public Accountants, prepared an "Auditability Assessment Report" under contract with Department of Defense Inspector General (DoD IG)

states that DIA cannot effectively address critical financial control activities until it fully documents its agency-specific accounting policies.

2. DoD IG prior reports on the Reliability of DIA Financial Statements and Processes (Report Number D-2004-079, 29 April 2004; Report Number 2003-74, 7 April 2003; Report Number D-2002-117, 25 June 2002).

Progress to Date: Established a CFO Act Compliance senior leader position and staffed. Established a Policy and Business Integration Office and staffed. Initiated development of formal financial policies with a targeted completion date of 31 December 2005.

Major Milestones:

1. Milestones for FY 2006: Completion of business rules and financial policies.
2. Milestones beyond FY 2006: Periodic updates of policies.

TAB C-2

REPORTABLE CONDITIONS

Lack of Documented Business Processes

Description of the Issue: Defense Intelligence Agency (DIA) does not have a complete set of documented business processes. To compound this problem, DIA relies on service providers in the area of financial management and accounting who manage and control certain business processes such as disbursing. Currently, DIA is migrating to an enterprise-wide accounting system and upgrading its functional support systems. In modernizing the functional systems, a business process redesign effort will take place and all of these efforts must be documented.

Functional Category: Comptroller/Resource Management

Pace of Corrective Action:

Year Identified: 2005
Original Targeted Correction Date: 4th Quarter FY 2006
Targeted Correction Date in Last Report: First time reported
Current Target Date: 4th Quarter FY 2006

Reason for Change in Dates: No change. First time reported.

Appropriation:

Title	Appropriation	FY2005	FY2006	FY2007	FY2008	Total
O&M	97x0100	\$0.4M	\$1.5M	\$1.0M	\$0.4M	\$3.3M

Validation Indicator: Initial indicator will be a set of business processes reflecting the current "as is" environment. Final indicator will be a documented set of financial processes depicting DIA's "to be" environment with the new Financial Management Solution (FMS).

Results Indicator: Documentation that enables an assessment of internal controls over financial reporting.

Source Documents: The following sources identified this issue:

1. Urbach Kahn and Werlin LLP, Certified Public Accountants, prepared an "Auditability Assessment Report" under contract with Department of Defense Inspector General (DoD IG) states that DIA cannot effectively address critical financial control activities until it fully documents its agency-specific accounting policies.

2. DoD IG prior reports on the Reliability of DIA Financial Statements and Processes (Report Number D-2004-079, 29 April 2004; Report Number 2003-74, 7 April 2003; Report Number D-2002-117, 25 June 2002).

Progress to Date:

1. Established and staffed a Policy and Business Integration Office.
2. Began documenting “as is” level 1-4 process maps.
3. Established and staffed an Internal Controls Office that began establishing assessable units, conducting risk assessments, and documenting key business process.

Major Milestones:

1. Milestones for FY 2006: Complete documentation of “as is” level 1-4 process maps.
2. Milestones beyond FY 2006: Complete documentation of “to be” level 1-4 process maps.

TAB C-2

REPORTABLE CONDITIONS

Lack of Implementing Procedures

Description of the Issue: Defense Intelligence Agency (DIA) has not established and not documented detailed implementing procedures to ensure all financial events are properly recorded in a timely manner. DIA uses service providers in the area of financial management and accounting. DIA must work with these service providers to ensure business processes are documented so that effective implementing procedures can be developed and documented.

Functional Category: Comptroller/Resource Management

Pace of Corrective Action:

Year Identified: 2005
Original Targeted Correction Date: 4th Quarter FY 2007
Targeted Correction Date in Last Report: First time reported
Current Target Date: 4th Quarter FY 2007

Reason for Change in Dates: No change. First time reported.

Appropriation:

<u>Title</u>	<u>Appropriation</u>	<u>FY2005</u>	<u>FY2006</u>	<u>FY2007</u>	<u>FY2008</u>	<u>Total</u>
O&M	97x0100	\$0.2M	\$1.5M	\$0.5M	\$0.3M	\$2.5M

Validation Indicator: Final indicator will be a completed, documented, and available set of implementing procedures for financial events. Interim progress is shown in the quarterly Chief Financial Executive (CFE) reports on improving financial performance for the President's Management Agenda scorecard.

Results Indicator: Progress in the quarterly update on the President's Management Agenda scorecard will indicate the documentation of specific implementing procedures as completed.

Source Documents: The following sources identified this issue:

1. Urbach Kahn and Werlin LLP, Certified Public Accountants, prepared an "Auditability Assessment Report" under contract with Department of Defense Inspector General (DoD IG) states that DIA cannot effectively address critical financial control activities until it fully documents its agency-specific accounting policies.

2. DoD IG prior reports on the Reliability of DIA Financial Statements and Processes (Report Number D-2004-079, 29 April 2004; Report Number 2003-74, 7 April 2003; Report Number D-2002-117, 25 June 2002).

Progress to Date:

1. Established and staffed a Policy and Business Integration Office.

Major Milestones:

1. Milestones for FY 2006: Documented set of implementing procedures for the current accounting system.
2. Milestones beyond FY 2006: Documented set of implementing procedures for the replacement accounting system.

TAB C-2

REPORTABLE CONDITIONS

Monitoring Unliquidated Obligations

Description of the Issue: Defense Intelligence Agency (DIA) has not reliably monitored unliquidated obligations. Several factors contribute to this condition including a lack of integrated financial information and an inability to reconcile with supporting contract and related documentation.

Functional Category: Comptroller/Resource Management

Pace of Corrective Action:

Year Identified: 2004
Original Targeted Correction Date: 4th Quarter FY 2006
Targeted Correction Date in Last Report: 4th Quarter FY 2006
Current Target Date: 4th Quarter FY 2006

Reason for Change in Dates: No change.

Appropriation:

<u>Title</u>	<u>Appropriation</u>	<u>FY2005</u>	<u>FY2006</u>	<u>FY2007</u>	<u>FY2008</u>	<u>Total</u>
O&M	97x0100	\$0.3M	\$1.3M	\$1.4M	\$1.5M	\$4.5M

Validation Indicator: Final indicator will be the successful and routine reconciliation of unliquidated obligations as part of the tri-annual review process. Interim progress is shown in the weekly data cleansing update. The update shows the total transactions and the amount of obligations reviewed. Quarterly, the Chief Financial Executive (CFE) reports on improving financial performance for the President's Management Agenda scorecard. And, monthly, the CFE provides progress updates to the Office of the Secretary of Defense (Comptroller) (OSD[C]) Mid-Range Financial Improvement Plan.

Results Indicator: Progress in the weekly data cleansing effort statistics show the amount of obligations reviewed.

Source Documents: The following sources identified this issue:

1. Urbach Kahn and Werlin LLP, Certified Public Accountants, prepared an "Auditability Assessment Report" under contract with Department of Defense Inspector General (DoD IG) states that DIA cannot effectively address critical financial control activities until it fully documents its agency-specific accounting policies.

2. DoD IG prior reports on the Reliability of DIA Financial Statements and Processes (Report Number D-2004-079, 29 April 2004; Report Number 2003-74, 7 April 2003; Report Number D-2002-117, 25 June 2002).

Progress to Date:

1. Established a CFO Act Compliance Senior Expert position and staffed.
2. Established a Comptroller Financial Statements position and office and staffed.
3. Established integrated data cleansing working group to integrate efforts between contractors and across Agency.
4. Established a review website with weekly data cleansing updates and metrics.
5. Drafted policy guidance and regulation.
6. Developed a training package on how to conduct reviews.
7. Developed metrics to track its progress in performing obligation reviews.
8. Preparing to implement policy of quarterly reviews to coincide with financial statements.

Major Milestones:

1. Milestones for FY 2006: Completed obligation reviews for all accounting lines.
2. Milestones beyond FY 2006: Perform reviews in accordance with the DoD Financial Management Regulation.

TAB C-2

REPORTABLE CONDITIONS

Reliability of Financial Information

Description of the Issue: Amounts reported on Defense Intelligence Agency (DIA) financial statements are unreliable. In particular material amounts reported as payables, receivables and property (and Fund Balance with Treasury (FBWT) which is reported separately as a material weakness in Tab B) did not have sufficient audit trails and supporting documentation. There is lack of formal financial policies and a lack of established and documented procedures which contributes to ineffective monitoring and reconciliation of detailed transactions to corresponding general ledger account balances.

Functional Category: Comptroller/Resource Management

Pace of Corrective Action:

Year Identified:	2004
Original Targeted Correction Date:	4 th Quarter FY 2006
Targeted Correction Date in Last Report:	4 th Quarter FY 2006
Current Target Date:	4 th Quarter FY 2006

Reason for Change in Dates: No change.

Appropriation:

<u>Title</u>	<u>Appropriation</u>	<u>FY2005</u>	<u>FY2006</u>	<u>FY2007</u>	<u>FY2008</u>	<u>Total</u>
O&M	97x0100	\$0.3M	\$1.3M	\$1.4M	\$1.5M	\$4.5M

Validation Indicator: Final indicator will be a successful audit of the balance sheet with an opinion being rendered on all the material amounts in the statement. Progress is also shown in annual Department of Defense Inspector General (DoD IG) financial statement reviews requested by the Senate Select Committee on Intelligence (SSCI). The reviews are supplemented by the SSCI requested "Annual Report on IC (Intelligence Community) Compliance with Federal Accounting Standards." Quarterly, the Chief Financial Executive (CFE) reports on improving financial performance for the President's Management Agenda scorecard. Monthly, the CFE provides progress updates to the Office of the Secretary of Defense (Comptroller) (OSD (C)) Mid-Range Financial Improvement Plan.

Results Indicator: Formalizing the policies and procedures for this area will indicate progress. Testing of the internal controls to ensure compliance with the policies and procedures should document the achievement of monitoring and reconciling the account balances.

Source Documents: The following sources identified this issue:

1. Urbach Kahn and Werlin LLP, Certified Public Accountants, prepared an "Auditability Assessment Report" under contract with DoD IG states that DIA cannot effectively address critical financial control activities until it fully documents its agency-specific accounting policies.
2. DoD IG prior reports on the Reliability of DIA Financial Statements and Processes (Report Number D-2004-079, 29 April 2004; Report Number 2003-74, 7 April 2003; Report Number D-2002-117, 25 June 2002).

Progress to Date:

1. Established a CFO Act Compliance Senior Expert position and staffed.
2. Established a Comptroller Financial Statements position and office and staffed.

Major Milestones:

1. Milestones for FY 2006: Documented set of implementing procedures for the current accounting system.
2. Milestones beyond FY 2006: Documented set of implementing procedures for the replacement accounting system.

TAB C-2

REPORTABLE CONDITIONS

Reliability of Financial Information (Property, Plant and Equipment (PP&E))

Description of the Issue: Information used to support the amounts reported in financial statements did not have sufficient audit trails and supporting documentation. Specific balance sheet items identified as requiring support were PP&E. For PP&E, deficient items included: (a) government-furnished equipment, (b) software, (c) computer systems, (d) Iraq Survey Group (ISG) equipment, (e) real property, (f) personal property and (g) defense attaché office property.

Functional Category: Supply Operations

Pace of Corrective Action:

Year Identified: 2004
Original Targeted Correction Date: 4th Quarter FY 2007
Targeted Correction Date in Last Report: 4th Quarter FY 2007
Current Target Date: 4th Quarter FY 2007

Reason for Change in Dates: No change.

Appropriation:

<u>Title</u>	<u>Appropriation</u>	<u>FY2005</u>	<u>FY2006</u>	<u>FY2007</u>	<u>FY2008</u>	<u>Cost to Complete</u>	<u>Total</u>
O&M	97x0100	\$7.5M	\$7.5M	\$3.0M	\$1.0M	\$3.0M	\$22.0M

Validation Indicator: Final indicator will be a successful audit of the balance sheet with an opinion being rendered on all the material amounts in the statement. Interim progress is shown in annual Department of Defense Inspector General (DoD IG) financial statement reviews requested by the Senate Select Committee on Intelligence (SSCI). The reviews are supplemented by the SSCI requested "Annual Report on Intelligence Community (IC) Compliance with Federal Accounting Standards." Quarterly, the Chief Financial Executive (CFE) reports on improving financial performance for the President's Management Agenda scorecard. Monthly, the CFE provides progress updates to the Office of the Secretary of Defense (Comptroller) (OSD(C)) Mid-Range Financial Improvement Plan. DIA IG site inspection reports show whether accountability is achieved at operations overseas.

Results Indicator: In process--not yet identified.

Source Documents: The following sources identified this issue:

1. DoD IG reports on the Reliability of DIA Financial Statements and Processes (Report Number D-2004-079, 29 April 2004; Report Number 2003-74, 7 April 2003; Report Number D-2002-117, 25 June 2002).

2. DIA OIG Inspection Reports (multiple).

3. DoD FY 2004 Performance and Accountability Report, Section 2, Systemic Weaknesses, "Department of Defense is unable to accurately report the value of property, plant, and equipment on its financial statements."

Progress to Date: DIA has taken steps to correct this material weakness. These steps include the proposed schedule:

Property, Plant, and Equipment.

1. Software.

31 July 2005: Policy on accounting for software.

30 June 2006: Capital software inventories.

30 June 2006: Post all capital software items to the property accounting records.

30 September 2005: Agency-level instruction issued.

2. Computer Systems.

31 July 2005: Policy on accounting for systems.

30 June 2006: Process and procedures guidance and task the inventory of systems.

30 September 2005: Complete Administrative Adjustment Reports and posting to the property accounting records.

30 September 2005: Agency-level instruction issued.

3. ISG Equipment.

Equipment transferred to the Multi-National Forces – Iraq.

4. Real Property.

31 July 2005: Policy on real property accounting.

31 July 2005: Process and procedures guidance for real property inventory.

On Going: All results of the real property inventory in the Office for Engineering and Logistics Services (DAL).

On Going: All applicable real property posted to the interim property accounting records (currently maintained in Excel, pending update of Property Accountability Support System (PASS) to accommodate real property).

30 September 2005: Update the Property Accountability Support System to accommodate real property inventory.

31 December 2005: Complete entry of all real property into PASS.

Major Milestones:

1. Milestones for FY 2006 (CFO Compliance Plan goal 7):

- a. 3rd Quarter 2006: Complete inventory of all software and record costs.
 - b. 3rd Quarter 2006: Complete inventory all systems and record costs.
 - c. 4th Quarter 2006: Complete Phase II (Regional Support Centers) of the wall to wall inventory of all personal property using the Radio Frequency Identification Device.
2. Milestones beyond FY 2006:
- a. 4th Quarter 2007: Property Asset Management Module (People Soft system).

TAB C-2

REPORTABLE CONDITIONS

Risk Assessment and Documentation in Acquisition Management

Description of the Issue: Until recently, Defense Intelligence Agency (DIA) used the Virginia Contracting Activity to provide contracting support for the Agency mission. Expert contracting officers have ensured the smooth operation of the organization. However, Acquisition Executive (AE) senior management is now assuming more responsibility in this role and is committed to ensuring that Agency dollars are well spent and free of waste, fraud, and abuse. Oversight of this role requires a much more stringent internal control program. To reduce acquisition risk to the Agency, the Acquisition Executive has contracted with Acuity Consulting, Inc., to conduct a risk assessment, identify AE assessable units, identify critical AE processes and the correct metrics for monitoring these processes, and ensure that these are documented. The end result will be improved management oversight and control and improved insight into the operation of all levels of AE.

Functional Category: Acquisition

Pace of Corrective Action:

Year Identified: 2005
Original Targeted Correction Date: 3rd Quarter FY 2006
Targeted Correction Date in Last Report: First Time Reported
Current Target Date: 3rd Quarter FY 2006

Reason for Change in Dates: No change. First time reported.

Appropriation:

<u>Title</u>	<u>Appropriation</u>	<u>FY2005</u>	<u>FY2006</u>	<u>FY2007</u>	<u>Total</u>
O&M	97x0100	\$0.2M	\$0.1M	\$0.1M	\$0.4M

Validation Indicator: Documentation of the critical AE processes and metrics that provide management with the key indicators required to monitor the organization and plan for its future.

Results Indicator: Indicators of key processes and assurance that the key processes are operating effectively, efficiently, and within the bounds of the law. The contractors will provide an Internal Control Assessment Report.

Progress to Date: Contractor began work in June of 2005 to identify assessable units and critical internal processes.

Major Milestones:

1. Milestones for FY 2006:

- a. Identification and Validation of assessable units and internal processes.
- b. Development and implementation of monitoring tools.
- c. Provision of Internal Controls Assessment Report.
- d. Completion of Acquisition Life Cycle Management Systems business process re-engineering effort.
- e. Implementation of re-engineering recommendations – improved business process.
- f. Selection of and business case for procurement package preparation capability.
- g. Selection of and business case for procurement support system.
- h. Assessment of Acquisition Security environment.

2. Milestones beyond FY 2006:

- a. Implementation of procurement package preparation capability.
- b. Implementation of procurement support system.