

UNITED STATES AIR FORCE

ANNUAL FINANCIAL STATEMENT

GENERAL FUNDS

FISCAL YEAR 1999

AUDIT OPINION



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2885

FEB 14 2000

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER) AND
CHIEF FINANCIAL OFFICER
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING
SERVICE

SUBJECT: Endorsement of the Disclaimer of Opinion on the FY 1999 Air Force General Fund Financial Statements (Project No. OFD-2111)

The Chief Financial Officers Act of 1990, as amended by the Federal Financial Management Act of 1994, requires financial statement audits by the Inspectors General. We delegated to the Air Force Audit Agency (AFAA) the audit of the FY 1999 Air Force General Fund financial statements. Summarized as follows are the AFAA disclaimer of opinion on the FY 1999 Air Force General Fund financial statements, report on internal controls, report on compliance with laws and regulations, and the results of our review of the AFAA audit. We endorse the disclaimer of opinion expressed by AFAA.

Disclaimer of Opinion. The AFAA disclaimer of opinion, dated February 9, 2000, on the FY 1999 Air Force General Fund financial statements states that AFAA was unable to express an opinion on the financial statements. We concur with the AFAA disclaimer of opinion that material uncertainties existed regarding the reasonableness of amounts reported on Air Force General Fund financial statements. Those uncertainties existed because of the following:

- The financial statements were not prepared in time for AFAA to perform necessary audit work before the reporting deadlines established by the Office of Management and Budget.
- The Air Force and the Defense Finance and Accounting Service did not implement the U.S. Government Standard General Ledger chart of accounts, and the systems used to account for funds did not employ a transaction-driven ledger to capture financial management information.
- The Air Force did not comply with Federal accounting standards because it used standard price to value operating materials and supplies, and it did not do the following:
 - report gains and losses on disposal of general property, plant, and equipment;
 - recognize holding gains and losses related to revaluations of operating materials and supplies;
 - revalue at their net realizable value operating materials and supplies (excluding munitions) identified as excess, obsolete, or unserviceable; and
 - fully use the consumption method of accounting for operating materials and supplies.

- The Air Force could not accurately identify all intragovernmental transactions by customer.
- The Air Force could not rely on closed year appropriation balances.
- The Air Force estimated that it still needed to determine the historical cost, accumulated depreciation, and acquisition date for \$895 million in General Fund equipment as of September 30, 1999.
- A backlog in recording real property transactions had caused real property values to be materially understated.
- The extent of environmental cleanup liabilities was uncertain because of incomplete documentation for cleanup cost estimates.
- The Air Force did not adequately document real property construction-in-progress of \$1.8 billion, which was reported by Army Corps of Engineers and Naval Engineering Command.
- The effects of the internal control weaknesses and noncompliance with laws and regulations that the Air Force and AFAA identified prevented completing substantive tests of material lines of the Statement of Budgetary Resources. The AFAA also could not confirm the ending obligated and unobligated balances on the Statement of Budgetary Resources for FY 1998; consequently, AFAA could not confirm the beginning balances on the FY 1999 statement.

Internal Controls. The AFAA tested internal controls but did not express a separate opinion on internal controls because that was not one of their objectives. However, AFAA determined that internal controls did not provide reasonable assurance of achieving the internal control objectives described in the Office of Management and Budget Bulletin, "Audit Requirements for Federal Financial Statements." We concur in the following material weaknesses and reportable conditions identified by AFAA.

- Internal reviews by Defense Finance and Accounting Service Columbus Center determined that access controls were inadequate over the conversion of contracts, invoices, and other original documents to electronic media in response to new DoD electronic commerce initiatives.
- Reporting of obligated balances were subject to material weakness because transaction records were not available and internal controls did not ensure proper matching of disbursements with related obligations.
- Supporting documentation controls over disbursements at the Defense Finance and Accounting Service Columbus Center were inadequate because center personnel could not promptly retrieve or provide documentation. Documentation provided could not be readily identified to the related transactions.
- Material control weaknesses existed in real property accounting because of inadequate application controls in the new Automated Civil Engineer System.
- The Contractor Property Management System used to report \$2.9 billion of Air Force operating materials and supplies did not distinguish between General Fund and Working Capital Fund assets or provide data in a timely manner.

We also concur that the audit trails for transactions reported on the financial statements did not meet internal control requirements. Although AFAA noted improvements in the reconciliation of transactions to financial statements, AFAA could not fully reconcile the transaction-level details reported at the field level, including those tested, to the financial statements. Transaction-level details supporting disbursements included in the Statement of Budgetary Resources did not reconcile to the financial statements. In other instances, AFAA could not complete other reconciliation tests because of the effects of the internal control weaknesses and instances of noncompliance with laws and regulations identified by the Air Force and the AFAA audit.

The Air Force and the Defense Finance and Accounting Service recognized many of the financial reporting weaknesses and reported them in their FY 1999 Annual Statements of Assurance. Details on the internal control weaknesses will be provided in separate AFAA reports.

Compliance With Laws and Regulations. We concur in the areas of noncompliance with laws and regulations that AFAA identified, which will be discussed in more detail in separate AFAA reports. Under the Federal Financial Management Improvement Act of 1996, the AFAA work showed that the financial management systems did not substantially comply with Federal financial management system requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level.

Review of Air Force Audit Agency Work. To fulfill our responsibilities for determining the accuracy and completeness of the independent work that AFAA conducted, we reviewed the audit approach and planning and monitored progress at key points. We also performed other procedures to determine the fairness and accuracy of the approach and conclusions.

We reviewed the AFAA work on the FY 1999 Air Force General Fund financial statements from October 27, 1999, through February 9, 2000, in accordance with generally accepted Government auditing standards.



David K. Steensma
Deputy Assistant Inspector General
for Auditing



DEPARTMENT OF THE AIR FORCE
WASHINGTON DC 20330-1000

OFFICE OF THE SECRETARY

9 February 2000

To the Secretary of the Air Force
Chief of Staff, USAF

We were engaged to audit the accompanying Air Force General Fund financial statements for the fiscal year (FY) ended 30 September 1999. The annual financial statements consist of the Balance Sheet and the related Statement of Net Cost, Statement of Changes in Net Position, Statement of Budgetary Resources, and Statement of Financing. Preparing these financial statements is the responsibility of the Defense Finance and Accounting Service (DFAS) and Air Force management. This report presents our opinion on the financial statements, evaluation on the effectiveness of internal controls over financial reporting, and assessment of compliance with laws and regulations.

OPINION ON THE FINANCIAL STATEMENTS

We are unable to express, and we do not express, an opinion on the Air Force Balance Sheet or the Statements of Net Cost, Changes in Net Position, Budgetary Resources, and Financing. We were unable to obtain sufficient, competent evidential matter, or apply other auditing procedures to satisfy ourselves as to the fairness of these statements under provisions of the *Government Auditing Standards* and Office of Management and Budget (OMB) Bulletin, Audit Requirements for Federal Financial Statements. Also, our audit work was impeded because the financial statements were not prepared in time to fully perform necessary audit work before the reporting deadlines established by the OMB. Material uncertainties exist regarding the reasonableness of amounts reported on these statements. Air Force management has disclosed many of these uncertainties as compliance or data problems in the financial statement notes. For example:

- DFAS and Air Force have not implemented the United States Government Standard General Ledger chart of accounts. Further, systems used to account for Air Force funds do not have a true transaction-driven general ledger to provide a consolidated source of financial management information for either management or financial statement purposes. (Financial Statement Note 1)
- The Air Force use of standard prices to value operating materials and supplies does not comply with federal accounting standards and does not report gains and losses on disposal of general property, plant, and equipment. The Air Force also does not

recognize holding gains and losses related to operating materials and supplies revaluation that occurs when standard prices are used. Also, except for munitions, the Air Force does not revalue operating materials and supplies at their net realizable value when they are identified as excess, obsolete, or unserviceable in accordance with Statement of Federal Financial Accounting Standards Number 3, Accounting for Inventory and Related Property, 27 October 1993. Finally, the Air Force does not fully use the consumption method of accounting for operating materials and supplies. (Financial Statement Notes 1 and 8)

- The Air Force cannot accurately identify all intragovernmental transactions by customer. (Financial Statement Note 1)
- Closed year appropriation balances are not reliable. (Financial Statement Note 1)
- Air Force management officials estimated that, as of 30 September 1999, the Air Force still needed to determine the historical cost, accumulated depreciation, and acquisition date for \$895 million in general fund equipment. (Financial Statement Note 9)

Other reasons for our disclaimer include a material understatement of real property value resulting from a backlog in recording real property transactions, and material uncertainties in the extent of environmental cleanup liabilities resulting from incomplete documentation of cleanup cost estimates. Further, we could not verify the accuracy of \$1.8 billion of \$2.8 billion construction-in-progress costs reported in the financial statements because the Air Force did not ensure the Army Corps of Engineers and Naval Facilities Engineering Command provided supporting documentation in sufficient detail to confirm the reported amounts.

In addition, we disclaim an opinion on the Statement of Budgetary Resources because of the effects of our FY 1998 disclaimer of opinion. We could not confirm the ending obligated and unobligated balances on that statement for FY 1998; consequently, we could not confirm the beginning balance on the FY 1999 statement. Efforts are ongoing to establish audited beginning period balances for FY 2000.

The Required Supplementary Information is not a required part of the basic financial statements but is supplementary information required by the Federal Accounting Standards Advisory Board and OMB Bulletin 97-01, Form and Content of Agency Financial Statements, 16 October 1996. We applied certain limited procedures to the deferred maintenance portion of this information; however, we did not audit the information and, therefore, express no opinion on it. Required Supplementary

Stewardship Information is also not a required part of the basic financial statements and is not required to be audited. However, we selectively tested additions and deletions of national defense property, plant, and equipment reported in the Required Supplementary Stewardship Information. We also express no opinion on the Required Supplementary Stewardship Information.

MANAGEMENT ACTIONS

In FY 1998, the Office of the Under Secretary of Defense (Comptroller/Chief Financial Officer) initiated strategies designed to produce auditable financial statements. Also, DFAS and the Air Force continued taking actions in FY 1999 to improve Air Force financial data accuracy and reporting in support of those initiatives. To illustrate:

- The Air Force and DFAS undertook extensive measures to improve the accuracy and auditability of budgetary data. Both organizations took actions to improve procedures related to periodic review of obligations, and DFAS worked with auditors to establish audit trails and reconcile field-level accounting transaction data to the departmental-level data used to prepare financial statements.
- The Air Force is working with DFAS to improve all accounting systems and “feeder systems” that provide financial data to the accounting systems. The Air Force has initiated the Financial Systems Information Assessment Study to identify functional and technical interactions among the financial systems serving the Air Force. The objective of this study is to remedy significant deficiencies and create an integrated set of systems to support Air Force business processes and financial reporting. To resolve the issues identified by this study and other actions, the Air Force has formed an Integrated Process Team composed of the subgroups responsible for corrective actions.
- During FY 1999, the Air Force fielded the real property module of the Automated Civil Engineer System at active Air Force bases and began using it for reporting real property asset information to the general ledger for financial statement preparation. Implementation for the Air National Guard will be completed in FY 2000.
- The Air Force continued to develop the Air Force Total Cost of Ownership information system to provide more details on weapon system support costs. The Air Force Vice Chief of Staff established a Steering Group to develop an overall plan for implementing Activity-Based Costing/Management to improve cost management. Further, in July 1999, DoD contracted with a major accounting firm to perform a DoD-wide study of cost accounting. The Air Force is presently evaluating the study results released in December 1999.

- The Air Force continued contracts initiated in FY 1998 with major accounting firms to ascertain the fair value of Air Force real and personal property. This effort includes validating all data being entered into the real property database and the Air Force Equipment Management System.
- The Air Force contracted with consultants to prepare and provide models for maintaining documentation to support costs for completing environmental restoration projects. Further, in November 1999, management provided interim guidance to commanders for preparing and maintaining cost estimate supporting documents. This effort is ongoing.
- The DFAS, with support from the Air Force, took action to improve end-of-period cut-off reporting to ensure expense and obligation transactions are reported in the period when they occur.
- The Air Force modified the Comprehensive Engine Management System programs, resulting in accurate identification and reporting of uninstalled engine gains and losses in FY 1999.

REPORT ON INTERNAL CONTROLS

Management is responsible for establishing and maintaining an internal control structure to provide reasonable, but not absolute, assurance that transactions are properly recorded, processed, and summarized to permit preparation of financial statements in accordance with federal accounting standards, and to permit safeguarding assets against loss from unauthorized acquisition, use, or disposal. Because of inherent limitations in any system of internal control, errors or fraud may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the effectiveness of the design and operation of policies and procedures may deteriorate. In addition, our consideration of internal control would not necessarily disclose all matters in the internal control that might be material weaknesses under auditing standards. A material weakness is a condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Although we accomplished internal control testing, our financial statement audit objectives did not include providing a separate internal control opinion; accordingly, we do not express such an opinion. However, the OMB Bulletin, Audit Requirements for Federal Financial Statements, requires that we describe reportable conditions and material weaknesses identified during the audit. Accordingly, the following paragraphs summarize material weaknesses and reportable conditions that existed in the design or operation of the internal control structure over financial reporting in effect at

30 September 1999 for the Air Force consolidated financial statements. These weaknesses, along with recommended remedial actions, time frames for corrective actions, and management comments, are more fully described in supporting audit reports issued separately to Air Force and DFAS management.

Electronic Commerce Initiatives

As part of a Deputy Secretary of Defense initiative designed to expand the use of new technologies, improve business practices, and make progress toward paperless contracting, DFAS is participating in a series of electronic commerce initiatives. These initiatives include Electronic Document Access (shared documents across DoD using the Internet), Electronic Data Interchange (computer to computer exchange of business information in a standard format), and Electronic Document Management (imaging to eliminate reliance on paper versions of documents such as invoices). Because they are not dependent on hard-copy, original source documentation, electronic commerce initiatives increase the possibility that fraudulent or erroneous information could enter the accounting and disbursement systems without being detected. Until independent auditors have reviewed these initiatives and their related internal controls, we must treat them as internal control weaknesses. The DoD Inspector General has scheduled a review of electronic commerce initiatives to commence during FY 2000.

Obligations

The process for reporting obligated balances is subject to material weaknesses because transaction records are unavailable and internal controls did not ensure proper matching of disbursements with related obligations. (Draft Report of Audit 00053011, Revenue and Other Financing Sources - Obligated Balances, FY 1999)

a. Obligations Incurred and Recoveries of Prior Year Obligations. DFAS accounting systems do not maintain individual transaction records of Air Force obligations incurred and recoveries of prior year obligations. Instead, the systems calculate totals for these types of transactions based upon net changes in obligated balances during the period. As a result, no transaction records are available for audit. Moreover, the totals for obligations incurred and recoveries of prior year obligations included on the Statement of Budgetary Resources at \$85.4 billion and \$2.2 billion, respectively, could be materially misstated because the accounting systems ignore individual increases and decreases which may have contributed to the calculated net change in obligations.

b. Matching Disbursements to Obligations. The DFAS internal controls did not ensure proper matching of disbursements with related obligations, resulting in \$327 million of negative unliquidated obligations in the accounting systems. Through electronic commerce initiatives and prevalidation of disbursements, DFAS and Air Force officials are working to resolve this long-standing internal control issue.

Audit Trails

Although DFAS actions resulted in dramatically improved audit trails this year, the audit trails, in our opinion, still do not meet internal control requirements. DFAS does not routinely reconcile field-level data to departmental summary records from which the financial statements are compiled, and DFAS management cannot readily reconstruct or duplicate the transactions and adjustments for validation purposes. Although we reconciled transactions we tested to the financial statements in most instances, management cannot have assurance that reported financial balances are correct without a permanent and easily determinable audit trail to the underlying transactions. Therefore, a significant risk exists that errors or irregularities may occur and not be detected within a timely period. (Draft Report of Audit 00053012, Revenue and Other Financing Sources – Adjustments and Reconciliations, FY 1999)

Supporting Documentation for Disbursements

The DFAS operating locations where we performed our audit continued to improve in producing supporting documentation. In nearly all cases, operating location personnel provided adequate supporting documentation for the disbursement transactions selected for audit. However, supporting documentation controls over disbursements at the DFAS Columbus Center were inadequate. Specifically, DFAS Columbus personnel were not able to promptly retrieve or provide documentation, and when provided, the documentation could not be readily identified to associated transactions. (Draft Report of Audit 99053004, Managerial Cost Accounting – Disbursements, FY 1999)

Real Property

Material control weaknesses existed in real property accounting. We determined application controls in the newly initiated Automated Civil Engineering System (ACES) needed strengthening in the areas of work orders, journal numbers, estimated value, additions and deletions, and facility usage. As a result of these control weaknesses, ACES did not capture estimated value costs of approximately \$392 million in the General Ledger with the resulting understatement of real property values. Of note, real property personnel at over half the locations audited stated they did not receive adequate training (50 of 99 locations) or receive sufficient written guidance related to ACES operations (51 of 99 locations). Further, 20 of the 99 locations audited were missing real property record documentation for periods ranging from 1 to 20 years, and we could not verify the accuracy and reliability of the real property database related to those specific locations and years. We attributed the control issues, in part, to the start up of ACES and believe some of the problems will be eliminated as implementation progresses. (Draft Report of Audit 99053006, Air Force Real Property, FY 1999)

Operating Materials and Supplies

We could not verify the accuracy of a material portion of operating materials and supplies. The Air Force and DFAS obtained \$2.9 billion (14 percent) of the Operating Materials and Supplies account balance from the Defense Logistics Agency's Contractor Property Management System. We could not verify the Operating Materials and Supplies account accuracy because the Contractor Property Management System does not distinguish between General Fund and Working Capital Fund assets or provide data in time to meet financial statement reporting milestones. (Draft Report of Audit 99053003, Inventory and Related Property, FY 1999)

Performance Measures

We did not identify any control weaknesses in our limited review of internal controls related to performance measures reported in the overview to the principal statements and notes. However, we only obtained an understanding of the sources and controls related to performance measures; our work was not intended to determine whether controls were in place and working as designed. Further, the Air Force is updating these measures to align them with its strategic plan. Finally, the information presented in the Overview was materially consistent with the financial statements and footnotes.

REPORT ON COMPLIANCE WITH LAWS AND REGULATIONS

Air Force management is responsible for complying with applicable laws and regulations. As part of obtaining reasonable assurance Air Force financial statements are free of material misstatement, we performed tests of Air Force compliance with certain laws and regulations where noncompliance could have a direct and material effect on determining financial statement amounts, including the requirements referred to in the Federal Financial Management Improvement Act (FFMIA), the Federal Managers' Financial Integrity Act (FMFIA), and the Statements of Federal Financial Accounting Standards (SFFAS). Our audit objectives did not include providing a separate opinion on overall compliance with laws and regulations and, accordingly, we do not express such an opinion.

However, the Federal Financial Management Improvement Act requires report disclosure on whether Air Force financial management systems substantially comply with federal financial management requirements, federal accounting standards, and the United States Government Standard General Ledger at the transaction level. To meet this requirement, we tested compliance using the guidance included in Appendix D of OMB Bulletin, Audit Requirements for Federal Financial Statements. We determined the Air Force and DFAS existing systems and controls did not enable full compliance with laws and regulations, which could have a direct and material effect on the FY 1999 Air Force financial statements. We considered the noncompliances reported below in forming our opinion on the FY 1999 Air Force consolidated financial statements. In addition, these weaknesses, along with recommended corrective actions, time frames for corrective actions, and management comments, are described in the cited supporting reports.

Federal Financial Management Improvement Act

The results of our tests disclosed instances, described below, where Air Force or DFAS systems did not substantially comply with the three Federal Financial Management Improvement Act requirements.

a. Federal Financial Management System Requirements. For FY 1999, our audits of the general and application controls of 8 Air Force General fund feeder systems and 5 DFAS-owned Air Force General Fund systems determined that 11 systems were deficient in the area of internal controls, 6 were deficient in accounting conformance, and 3 were deficient in other legal requirements. The primary system control weaknesses identified in the eight feeder systems examined were audit trails (six systems), access controls (five systems), configuration management (four systems), completeness (four systems), and accreditation (three systems).

b. Federal Accounting Standards. For FY 1999, Air Force management acknowledged its financial management systems did not substantially comply with federal accounting standards. Specifically, footnotes to the principal statements stated the Air Force did not: use the correct basis to value material and equipment; recognize gains and losses on disposal of general property, plant, and equipment; recognize holding gains and losses related to the revaluation of operating materials and supplies; except for munitions, revalue operating materials and supplies at their net realizable value when identified as excess, obsolete, or unserviceable; or use the consumption method of accounting for operating materials and supplies. The Air Force also recognized that government property in the possession of contractors cannot be accurately reported, all intragovernmental transactions by customers cannot be accurately identified, and closed-year appropriation balances are not reliable. We identified additional departures from federal accounting standards which are detailed later in this report.

c. US Government Standard General Ledger at the Transaction Level. Air Force and DFAS managers did not use the US Government Standard General Ledger at the transaction level. Further, financial statement footnotes disclose that the Air Force and DFAS have not implemented systems that use a true transaction-driven general ledger process. Because DFAS did not have a transaction-driven general ledger process, data were extracted from multiple automated and manual systems to determine account balances, significantly increasing the potential for account balance misstatements.

Federal Managers' Financial Integrity Act

The Air Force acknowledged in its FY 1999 Statement of Assurance that Air Force systems do not fully comply with federal financial management systems requirements. The Report on Air Force Critical Financial Management Systems in the Statement of Assurance identifies the 40 systems that provide significant information to the DFAS accounting systems that produce the Air Force financial reports. The report describes the actions under way to bring these systems into conformance with federal financial management system requirements. These improvement efforts were also incorporated

into the DoD Financial Management Improvement Plan. All material weaknesses disclosed by our audit were reported in either the Air Force, DFAS-Denver, or DFAS Headquarters Statement of Assurance for FY 1999.

Statements of Federal Financial Accounting Standards

For FY 1999, the financial management systems that support the Air Force did not substantially comply with federal accounting standards. In addition to the issues disclosed above, we identified the following departures from the SFFAS requirements.

a. Consumption Accounting. Air Force logistics personnel had not fully implemented the consumption method of accounting to recognize all inventory and related property expenses, as required by SFFAS Number 3, Accounting for Inventory and Related Property, 27 October 1993. The Air Force cannot use the consumption method because its computer systems were designed for inventory control purposes rather than financial accounting purposes. Therefore, the Air Force systems and processes prevent accounting personnel from determining whether the changes in value between accounting periods resulted from expenses relating to operating materials and supplies or from purchases, issues, and price changes. The DoD has initiated action to move to the consumption method of accounting in future years except in those cases that meet the requirement for the purchase method as defined in SFFAS Number 3. (Draft Report of Audit 99053003)

b. Cost Accounting. As we reported last year, Air Force and DFAS personnel did not prepare the Statement of Net Cost in full conformance with SFFAS Number 4, Managerial Cost Accounting Concepts and Standards for the Federal Government, 31 July 1995. Deviations from the standard occurred in the areas of reporting program costs and reporting by responsibility segments. Air Force and DFAS management disagreed with our audit results last year and did not change the way they prepared the Statement of Net Cost for FY 1999. We forwarded both issues to the DoD Inspector General for resolution, but neither issue was resolved at the time of this report.

c. Construction-In-Progress. Air Force real property personnel did not always comply with Federal recognition requirements in accounting for real property. Specifically, real property personnel did not capitalize facilities at the time they were placed in service at 46 of 99 locations as directed by SFFAS Number 6, Accounting for Property, Plant and Equipment, 30 November 1995. Consequently, at least 511 facilities or projects valued at \$100,000 or more, with a total value of approximately \$781 million, were not recorded in the real property records and may not be recorded in the FY 1999 consolidated financial statements. (Draft Report of Audit 99053006)

Objective, Scope, and Methodology

Management's responsibilities are to:

- Prepare the annual financial statements in conformity with applicable accounting principles.
- Establish and maintain internal controls and systems to provide reasonable assurance that the broad control objectives of the FMFIA are met.
- Implement and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger at the transaction level.
- Comply with other applicable laws and regulations.

Air Force Audit Agency responsibilities are to:

- Plan and perform an audit to obtain reasonable assurance about whether the principal financial statements are reliable (free of material misstatement) and presented fairly in conformity with Office of Management and Budget (OMB) Bulletin 97-01, Form and Content of Agency Financial Statements, and applicable accounting principals.
- Obtain reasonable assurance about whether relevant management internal controls are in place and operating effectively.
- Test management's compliance with selected provisions of laws and regulations and perform limited procedures to test the consistency of other information presented with the consolidated financial statements.

To fulfill these responsibilities, we:

- Examined, on a test basis, evidence supporting the amounts and disclosures in the principal financial statements.
- Assessed the accounting principles used and significant estimates made by management.
- Evaluated the overall presentation of the financial statements.
- Tested compliance with selected provisions of laws and regulations.
- Obtained sufficient evidence from our tests to support our assessment of internal controls.

- Performed the procedures described in the Codification of Statements on Auditing Standards, AU Section 558, Required Supplementary Information, as they apply to the reporting of deferred maintenance.
- Selectively tested evidence supporting additions, deletions, and disclosures in the Required Supplementary Stewardship Information.
- Followed up on previously reported deficiencies.

In reviewing the Air Force consolidated financial statements, we evaluated internal controls to determine the reliability of financial and performance reporting related to the principal statements, accompanying footnotes, and the Overview of the Reporting Entity, including performance measures.

In the area of financial reporting, we determined whether Air Force and DFAS personnel properly recorded, processed, and summarized transactions to permit the preparation of financial statements in accordance with federal accounting standards. We also evaluated the safeguarding of assets against loss from unauthorized acquisition, use, or disposition; obtained an understanding of the design of internal controls; determined whether the controls were in operation; assessed control risk; and tested the controls.

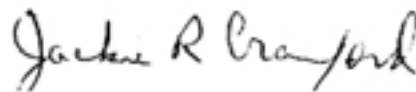
With respect to information in the Overview of the Reporting Entity, we determined whether the information presented was materially consistent with the information presented in the Principle Statements and accompanying footnotes. In the area of performance measures, we determined whether Air Force personnel properly recorded, processed, and summarized transactions and other data that support performance measures included in the overview accompanying the Air Force consolidated financial statements. We obtained an understanding of the design of internal controls related to the existence and completeness assertions.

We accomplished the audit from January to December 1999 at the Office of the Assistant Secretary of the Air Force, Financial Management and Comptroller; DFAS locations (DFAS centers and DFAS operating locations); HQ Air Force Materiel Command; and Air Force active duty units. We listed specific locations in the individual audit reports. We completed audit field work in February 2000 and provided a draft report to management in February 2000.

Summary of Prior Audit Coverage

The General Accounting Office (GAO), Inspector General, Department of Defense (IG, DoD), and the Air Force Audit Agency (AFAA), have conducted multiple reviews related to financial management issues. Last year, we issued a disclaimer on the FY 1998 Air Force consolidated financial statements. GAO reports can be accessed over the Internet at <http://www.gao.gov>, IG, DoD reports can be accessed at <http://www.dodig.osd.mil>, and AFAA reports can be accessed at <http://www.afaahq.af.mil>.

We appreciate the cooperation and courtesies extended to our auditors.



JACKIE R. CRAWFORD
The Auditor General