UNITED STATES DEPARTMENT OF DEFENSE

FINANCIAL IMPROVEMENT AND AUDIT READINESS (FIAR) PLAN

Status Report

May 2010

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

Message from the Under Secretary of Defense (Comptroller)

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

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

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

Robert F. Hale
Under Secretary of Defense (Comptroller)

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Executive Summary

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

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

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

PROGRESS MADE BUT CHALLENGES REMAIN

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

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

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

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

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

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

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

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

SIGNIFICANT CHANGES HAVE BEEN MADE

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

- Budgetary information, and
- Mission critical asset information.

The USD(C) also directed the Components to aggressively modify their Financial Improvement Plans (FIPs) to address these priorities. The individual Component FIPs, when summarized collectively, are the Department's FIAR Plan. The results of the Components' efforts to update their FIPs are reflected in this Report. The Components' plans continue to be modified, while work commences on the priorities. The November 2010 FIAR Plan Status Report will provide additional and more detailed information filling gaps that presently exist in the Components' plans. The Department also will add plans for organizations not yet reflected in the FIAR Plan.

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

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

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

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

Figure 1. FY 2010 – FY 2014 FIAR Budget

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

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

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

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

FIAR STATUS AND LONG-TERM AND INTERIM MILESTONES

The amount of work to be done by the Military Departments and Defense Agencies to correct long-standing material weaknesses, test and strengthen controls, and modernize business and financial processes and systems is enormous. It requires an incremental and prioritized strategy and phased methodology with visibility of ongoing and planned actions by those executing the FIPs and those overseeing their execution. To overcome these challenges and focus the Department's limited financial improvement resources on the prioritized objectives, the FIAR Strategy, explained in Section I, aligns improvement work into three waves. The three waves are:

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

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

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

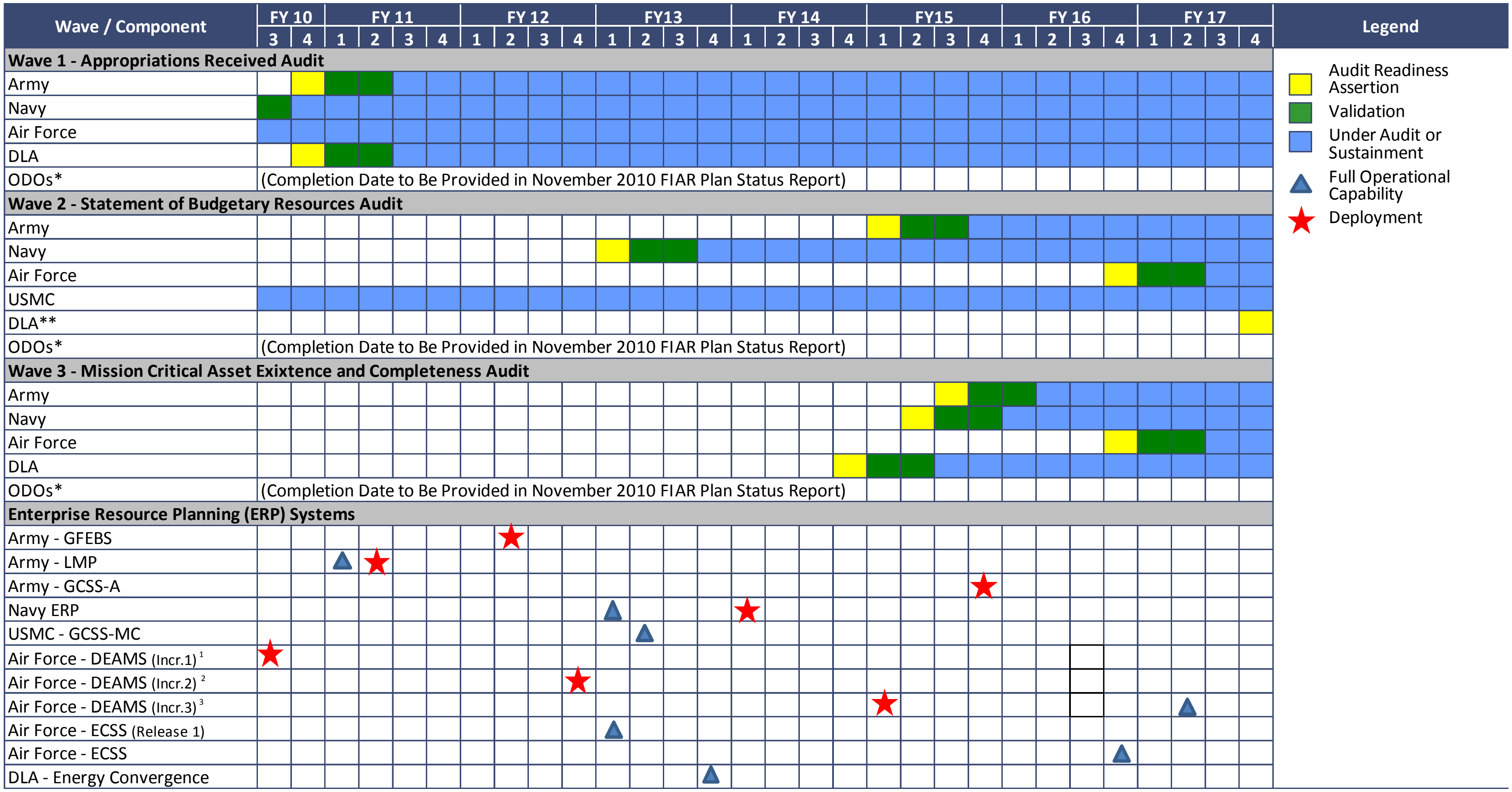
As shown in Figure 2, the Army is planning to assert audit readiness for the SBR in the first quarter of FY 2015. The Navy is planning to assert SBR audit readiness in the first quarter of FY 2013. The Air

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

Other than DLA, Figure 2 does not reflect the plans of any other Defense Agencies or organizations. The Department has analyzed the composition of the DoD Combined SBR to determine all Defense Agencies and other Defense organizations that materially impact the SBR and has begun working with many of them to achieve the objectives of Wave 2. At the time of this Report, the other Defense Agencies and organizations do not have FIPs that conform to the FIAR Audit Readiness Strategy and Methodology. The November 2010 FIAR Plan Status Report will be more inclusive of all Defense organizations that must be included in order to achieve auditability of the DoD Combined SBR.

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

Figure 2. Audit Readiness Wave and ERP Milestones



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

Figure 3. Interim Audit Readiness Goals

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

Legend
- Audit Readiness Assertion
- Validation
- Under Audit or Sustainment
- Capability to Reconcile

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

- Military and General Equipment (ME and GE),
- Real Property,
- Inventory, and
- Operating Materials and Supplies (OM&S).

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

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

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

ACHIEVING FULL AUDITABILITY

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

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

Other concurrent improvement activity, such as the deployment of the ERPs also supports achieving full auditability. The Department intends to ensure successful ERP implementation, because they are critically needed for business operations, as well as financial improvement and auditability.

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

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

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

CONCLUSION

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

I. The FIAR Strategy

The Financial Improvement and Audit Readiness (FIAR) Plan defines the Department's strategy and methodology for improving financial management, prioritizing improvement activity, strengthening internal controls, and achieving auditability. With the inception of a new Administration and in accordance with Section 1003 of the National Defense Authorization Act (NDAA) for Fiscal Year 2010, the FIAR Plan has undergone noteworthy changes.

This Report summarizes the actions and plans of the Components towards achieving auditability, updates the Department's progress towards achieving audit readiness, improving financial management, and increasing efficiency in financial operations. It also provides a thorough account of the changes to the FIAR Plan, which includes:

- Clarified goals,
- Focused objectives and priorities,
- Increased resources,
- Revised audit readiness strategy,
- More detailed, phased methodology, and
- Increased governance.

Detailed information on each of these changes is provided in the sections that follow. In addition, this section of the Report concludes with charts and discussion on the Components' audit readiness goals and milestones, and a section pertaining to achieving auditable financial statements.

GOALS

The FIAR strategy has evolved and matured since the plan was first issued in 2005. Its evolution, based on lessons learned, now encompasses the breadth of process, control, and system improvements required and more fully addresses internal control testing and remediation efforts. This strategy supports the portion of the Office of the Under Secretary of Defense (Comptroller) (OUSD(C)) mission to:

Improve business and financial processes, controls, systems and data to achieve accurate, reliable and timely financial and managerial information for decision makers and citizens.

The Department's FIAR goals in support of this mission are to:

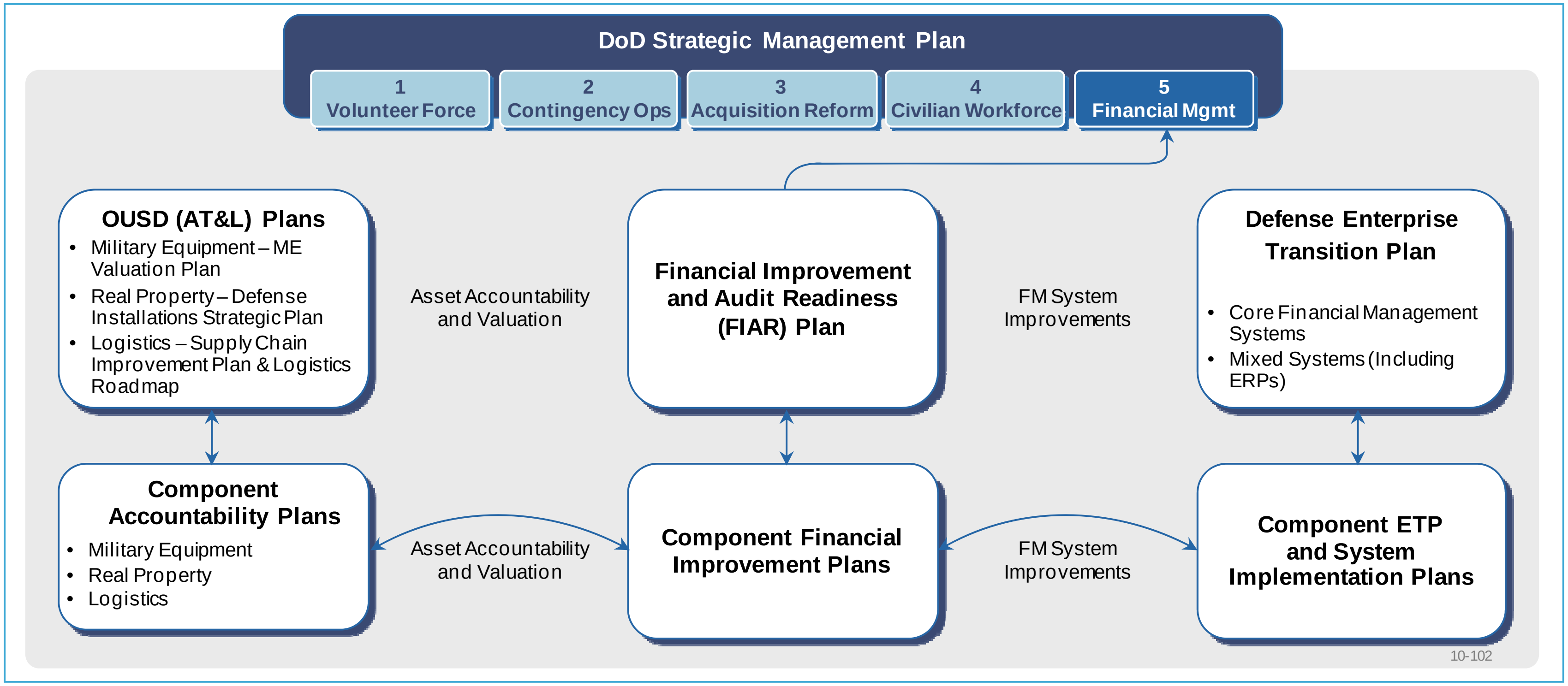
- Achieve and sustain audit readiness,
- Achieve and sustain unqualified assurance on effectiveness of internal controls, and
- Attain Federal Financial Management Improvement Act (FFMIA) compliance – financial management systems that support effective financial management

The FIAR Directorate has the responsibility to work with various offices of the Department and its Components to realize this mission and these goals by providing value-added leadership, guidance and ongoing monitoring. The FIAR Plan, in alignment with the DoD Strategic Management Plan (SMP), is focused on improving financial information, standardizing the Component's Financial Improvement Plans (FIPs), identifying critical financial management capabilities, increasing accountability for improvement tasks, developing new metrics for monitoring progress, and identifying the resources being applied to and needed for improvement activity.

DoD Strategic Management Plan

The DoD SMP, a requirement of the NDAA for Fiscal Year 2008, established five top-level priorities for business operations. Business Priority 5, "Strengthen DoD Financial Management," establishes required outcomes, goals, measurements, and key initiatives to ensure DoD leaders have access to timely, relevant and reliable financial and cost information.

Figure I-1. FIAR Plan Relationship to the DoD Strategic Management Plan and Other DoD Plans



As shown in Figure I-1, the FIAR Plan provides the strategy and methodology to achieve the outcomes of SMP Business Priority 5 by integrating the Component FIPs with the other key DoD plans, OUSD(AT&L) Plans, Component Accountability Plans, Defense Enterprise Transition Plan (ETP), and Component ETP and System Implementation Plans. The outcomes, goals and measures associated with this Business Priority focus on improving financial information for fact-based, actionable management decisions and achieving auditable financial statements.

One of the outcomes of Business Priority 5 is to "Demonstrate good stewardship of public funds." The USD(C) is responsible for achieving this outcome and the associated goal to "Increase the audit readiness of individual DoD Components." The Business Priority 5 key initiatives that drive achieving auditability are:

- Launch the new FIAR strategy, and
- Re-synchronize ETP milestones to support a revised FIAR strategy.

The FIAR Plan and Component FIPs have been synchronized with their ETP milestones to achieve the FIAR goals. The FIAR strategy and priorities are discussed in this Report.

OBJECTIVES AND PRIORITIES

The priorities within the FIAR Plan were established by the USD(C) on August 11, 2009. Soon after Senate confirmation, the USD(C) met with senior leaders across the Department to help shape his objectives and priorities for the Department's financial improvement activities. Before revising the Department's priorities, the USD(C) coordinated them with the Deputy Secretary of Defense and Components, Office of the Inspector General (OIG), Office of Management and Budget (OMB), Government Accountability Office (GAO), and Congress, who approved, endorsed or acknowledged them.

The objective of the priorities, as established by the USD(C), requires the Components to first focus on improving processes and controls supporting information that is most often used to manage the Department, while continuing to work toward financial improvements that permit receiving unqualified audit opinions on their financial statements. To achieve that objective, the USD(C) assigned a high priority to:

- Budgetary information, and
- Mission critical asset information.

The USD(C) also directed the Components to aggressively modify their FIPs to conform to the new objective and priorities. This Report presents the progress made to date to meet this objective.

Budgetary Information

Recognizing that many decisions made in the Department are budget related (e.g., status of funds received, obligated and expended), the first priority set by the USD(C) focuses improvement effort on processes, controls and systems that produce budgetary information. By focusing improvement activity on budgetary information and ensuring it is timely and accurately produced, the Department will accomplish the USD(C) objective to improve information most often used by management and also meet the goal of obtaining auditable financial statements starting with the Statement of Budgetary Resources (SBR).

The benefits of focusing improvement efforts on budgetary information and the SBR include:

- Improving the visibility of budgetary transactions resulting in more effective use of resources,
- Providing for operational efficiencies through more readily available and accurate cost and financial information,
- Improving fiscal stewardship (ensures that funds appropriated, expended and recorded are reported accurately, reliably and timely),
- Improving budget processes and controls (reduces Antideficiency Act violations), and
- Linking fund execution to the President's Budget (more consistency with the financial environment).

There are many challenges that the Department must overcome to achieve this priority. They include:

- The budgetary and financial environment must be evaluated, which includes a thorough understanding of business processes, controls, and systems, many of which are in the process of changing.
- Suballotments, disbursement by others, and bulk obligations must be evaluated and problems with timely and accurate recording of these budget actions must be corrected.
- Each Component is in a different stage of developing and deploying an integrated financial management system that results in changes to processes and controls.
- The functional (e.g., Logistics) communities' business environment must be understood, assessed and evaluated since their business events trigger financial transactions (e.g., receipt of goods and services is often not recorded in the general ledger).
- Documentation that supports events and transactions must be evaluated and actions taken to ensure it is properly retained and made readily available for audits. Transaction level detail is critical to success, and documentation supporting prior year transactions will be difficult and time consuming to locate and prepare for audit.

- The support provided by third party service providers must be understood, evaluated and assessed, because they play key roles within business and financial environments of the Components.

These challenges are not new and the Department has been addressing them. However, the challenges will need to be worked aggressively to continue to identify and resolve deficiencies that impede success toward achieving this important priority.

Mission Critical Asset Information

The second priority established by the USD(C) focuses improvement and audit readiness work on information essential to effectively manage the Department's mission critical assets. For purposes of this priority, mission critical assets include:

- Military Equipment (e.g., ships, aircraft, combat vehicles)
- Real Property (e.g., land, buildings, structures, utilities)
- Inventory (e.g., rations, supplies, spare parts, fuel)
- Operating Materials and Supplies (e.g., ammunition, munitions)
- General Equipment (e.g., training equipment, special tooling and test equipment, shipyard cranes)

Some of the same information needed to manage the Department's mission critical assets is also needed for future financial statement audits. Such information includes:

- Unique Identifiers (e.g., item unique identification [IUID] number, Real Property UID [RPUID], aircraft tail number, ship number)
- Location (e.g., military installation/base)
- Condition (e.g., operational status/in-service)
- Accountable organization (e.g., 374th Tactical Airlift Wing)
- Accountable individual (e.g., SSGT John Smith)

This above information, and much more management and financial information, will be recorded in the Department's official system of record, referred to as "Accountable Property System of Record" (APSR). Ensuring that important management information regarding mission critical assets is accurately recorded in each Component's specific APSR is the objective of this priority.

The benefits of focusing improvement efforts on mission critical asset information include:

- Moving the Department closer to achieving its long-standing goal of total asset visibility.
- More reliable and accurate logistics supply chain and inventory systems.
- Improved ability to timely acquire, maintain and retire assets.
- More effective utilization of assets.
- Better control over assets preventing their misuse, theft or loss.
- Reducing unnecessary reordering.

Accomplishing this priority will not only improve important management information, it will also move the Department closer to auditability as existence and completeness of assets are two of the five financial statement assertions that auditors test in a full financial statement audit.

RESOURCES

Resources for financial improvement and audit readiness activities have competed with other high priorities, such as the Overseas Contingency Operations, resulting in limited funding for FIAR requirements. Lack of resources has been a serious impediment to FIAR progress except in the Navy and DLA, which have been more successful at budgeting for financial improvement efforts, and where more progress has been made compared to the other Components.

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

The financial improvement activities funded by the budgets in Figure I-2 include assistance and oversight by the Office of the USD(C) FIAR Directorate; performing evaluation and discovery; defining, designing and implementing an audit ready environment; documenting, modifying or implementing new processes and controls; testing and strengthening controls; validating and ensuring the availability of supporting transaction documentation; data cleansing; and asserting audit readiness. The Navy amounts also include funds for audits while DLA amounts include funds for Service Provider audit readiness support such as DFAS internal control testing.

The amounts identified in Figure I-2 do not include budgets for systems modernization.

Figure I-2. FY 2010 – FY 2014 FIAR Budget

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

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

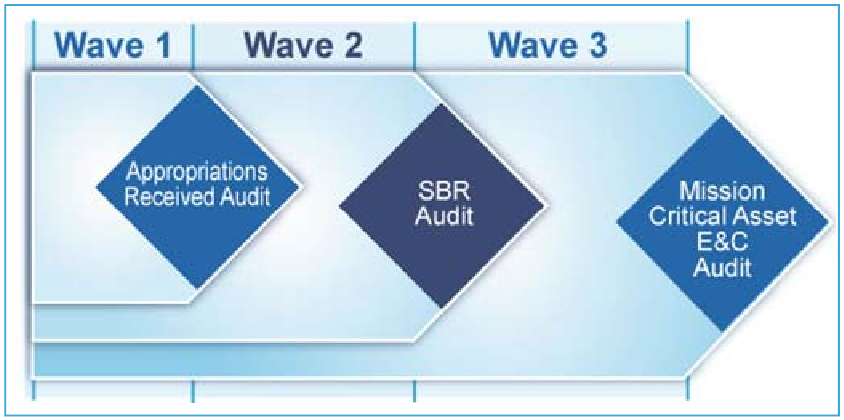
The additional resources, which will become available next fiscal year, will have a significant impact in the Department's ability to resolve its long-standing financial management deficiencies and material weaknesses and achieve the FIAR goals, objectives and priorities.

FIAR AUDIT READINESS STRATEGY

A clear, comprehensive strategy for achieving the FIAR goals and objectives is critical to ensuring limited resources are assigned effectively to facilitate sustained and measurable progress. The FIAR Audit Readiness Strategy provides a critical path organized by five waves of focused assessment and improvement activities while balancing the need to achieve short-term accomplishments with the long-term goal of an unqualified opinion on the Department's financial statements. Additional information on the FIAR Audit Readiness Strategy is provided in Appendix 1.

The FIAR Audit Readiness Strategy is consistent with and focuses improvement work on the priorities established by the USD(C): Wave 1, Wave 2 and Wave 3, as shown in Figure I-3. The three waves are being worked concurrently because they focus on both of the USD(C)'s priorities, budgetary information and mission critical asset information.

Figure I-3. FIAR Audit Readiness Strategy Includes Three Waves to Achieve the USD(C) Priorities



Wave 1 – Appropriations Received Audit focuses on activity reported on the Budget Authority section of the Statement of Budgetary Resources (SBR). This SBR section includes the funding appropriated by Congress for the current fiscal year and related apportionment/re-apportionment activity by the Office of Management and Budget (OMB).

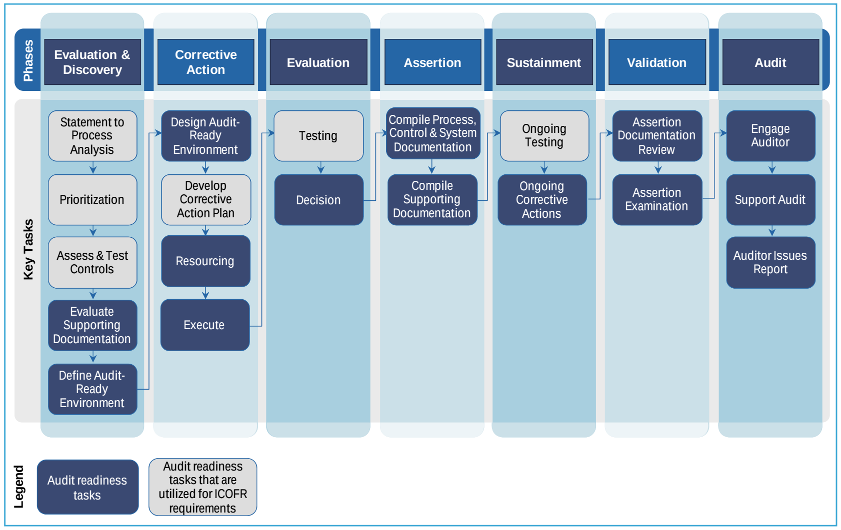
Wave 2 – SBR Audit includes all processes, internal controls, systems and supporting documentation that must be audit ready before the SBR can be audited. Audit readiness activities executed in line with these established priorities allow for the successful completion of dependencies necessary for remediation of subsequent line items. Significant processes in this wave include Procure-to-Pay, Hire-to-Retire, Order-to-Cash and Budget-to-Report, in addition to Fund Balance with Treasury.

Wave 3 – Mission Critical Asset Existence and Completeness Audit focuses primarily on the Existence and Completeness (E&C) financial statement assertions, but also includes the Rights assertion and portions of the Presentation and Disclosure assertion. That is, Components must ensure that all assets recorded in their accountable property systems of record exist (Existence), all of the Components' assets are recorded in their system (Completeness), and Components have the right to report all assets (Rights). The asset categories included in this wave include Military Equipment (ME), Real Property (RP), Inventory, Operating Materials and Supplies (OM&S) and General Equipment (GE).

METHODOLOGY

Before the issuance of the FIAR Plan in 2005, the Department developed "Business Rules" that required the Components to execute a phased methodology to achieving auditability. The Business Rules also established a methodology for the OUSD(C) and OIG to evaluate the audit readiness of a Component before a financial statement audit was to be performed. The Business Rules ensured the potential for successful financial statement audits. The Business Rules have been modified and expanded to include Key Tasks (with underlying detailed

Figure I-4. FIAR Methodology Phases and Key Tasks



Note: A larger version of this graphic is located in Appendix 1.

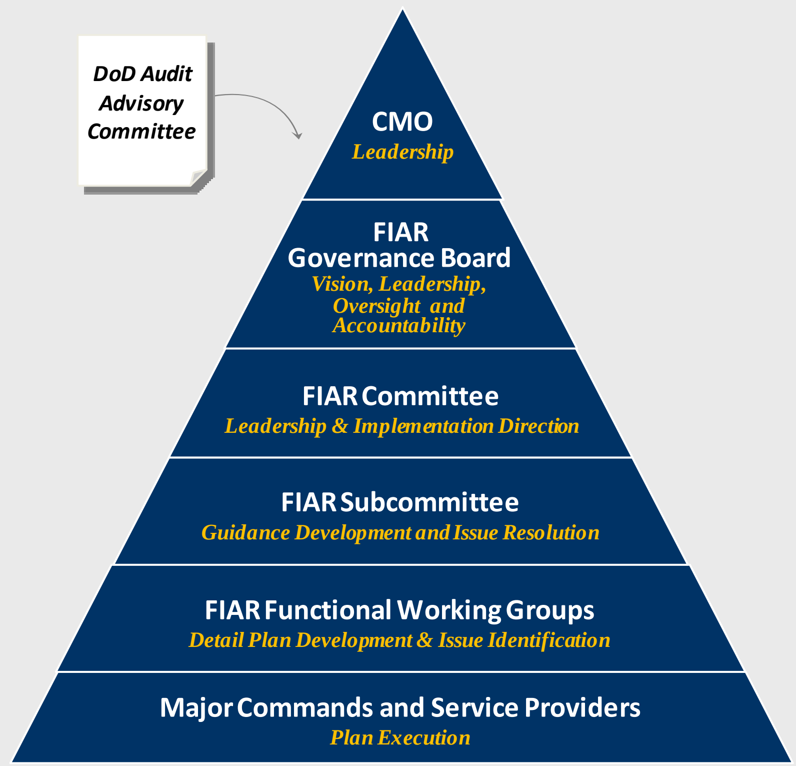
activities and resulting work products). The Business Rules are now referred to as Phases within the FIAR Methodology, as depicted in Figure I-4. Additional information on the Methodology can be found in Appendix 1.

GOVERNANCE

The Department has established a governance structure that engages all of the key stakeholders. Figure I-5 provides a graphical representation of the governance structure, the participants and their roles.

The USD(C) provides the vision, goals and priorities of the FIAR Plan, which are coordinated with key stakeholders within the Department (e.g., Military Departments), as well as outside the Department (OMB and Congress). The Deputy Secretary of Defense /Chief Management Officer (CMO) approves the vision, goals and priorities.

Figure I-5. FIAR Goverance



Leadership	• CMO
Vision, Leadership, Oversight & Accountability	• USD(C)/CFO, DCMO, MILDEP DCMOs, MILDEP FM/C Asst Secretaries, DCFO, DFAS Director, DLA DepDir
Leadership & Implementation Direction	• DCFO, FIAR Director, AT&L Directors, MILDEP FM/C Deputy Asst Secretaries, DFAS DepDir, DLA Compt, DoD IG (Advisory Member)
Guidance Development & Issue Resolution	• FIAR Director, Senior Staff of AT&L, Component FM and Functional Offices, DoDIG (Advisory Member)
Detail Plan Development & Issue Identification	• FIAR Staff, Staff of AT&L, Component FM and Functional Offices
Plan Execution	• Major Commands, Service Providers

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FIAR Governance Board

The FIAR Governance Board, which was established in FY 2010, replaces the Financial Management Leadership Council, and expands the participants to include the DoD DCMO and Military Department DCMOs. The FIAR Governance Board engages the Department's most senior leaders from the financial management community along with the DCMOs. The DCMOs have cross-community (business and financial) responsibilities and authority to transform budget, finance and accounting operations and to eliminate or replace financial management systems that are inconsistent with transformation. The Board is chaired by the USD(C).

The FIAR Governance Board meets quarterly and reviews Component progress. Accountability for progress begins at the top and is a key role of the Board. The Board's governance role also provides the Department with a visible leadership commitment, which is critical to achieving the FIAR goals and objectives.

FIAR Committee and Subcommittee

The Department also looks to the FIAR Committee, which meets monthly, to oversee the management of the FIAR Plan. The FIAR Committee leads the implementation of the FIAR Plan priorities. Chaired by the Deputy Chief Financial Officer (DCFO), the Committee is comprised of executive-level representatives of the Office of the Under Secretary of Defense (Acquisition, Technology and Logistics (OUSD(AT&L)), Military Departments, Defense Logistics Agency (DLA), Business Transformation Agency (BTA), and Defense Finance and Accounting Service (DFAS). The Deputy Inspector General for Auditing acts as an adviser to the FIAR Committee. An active FIAR Subcommittee of senior accountants, financial managers, management analysts, and auditors support the FIAR Committee. The Subcommittee assists the FIAR Directorate, OUSD(C) in developing detailed guidance and resolutions to issues. This collaborative management structure ensures the FIAR Plan is comprehensive with regard to DoD-wide organizations, issues and solutions.

FIAR Directorate and Functional Working Groups

To manage the FIAR Plan and ensure that DoD-wide financial improvement efforts continue to mature and are integrated with transformation activities across the Department, the OUSD(C) established the FIAR Directorate, a program management office. The FIAR Directorate:

- Recommends strategic direction to the DCFO and USD(C),
- Assists the Components where possible,
- Develops and issues detailed financial improvement and audit preparation methodologies and guidance,
- Organizes and convenes cross-Component financial and functional working groups to assist in developing the audit readiness methodology and process,
- Utilizing experienced financial, accounting and auditing personnel, embeds teams to develop, improve and execute FIPs and provide training to Components,
- Biannually, publishes the FIAR Plan Status Report,
- Maintains the FIAR Planning Tool, which is used by the Components to manage their FIPs,
- Monthly, performs detail reviews of the Component FIPs supported by the OUSD(AT&L) and provides feedback to the Components, as needed, and
- Develops metrics for monitoring and reporting progress.

Major Commands and Service Providers

It is Components' major commands and Service Providers, such as the Army Materiel Command (AMC) and Defense Finance and Accounting Service (DFAS), where the FIPs are executed. The major commands and Service Providers perform the evaluation and discovery work, test and strengthen internal controls and correct deficiencies. It is within the major commands where business events occur that trigger financial transactions, and where the functional community engages with the financial community to achieve the vision, goals and priorities of the FIAR Plan.

DoD Audit Advisory Committee

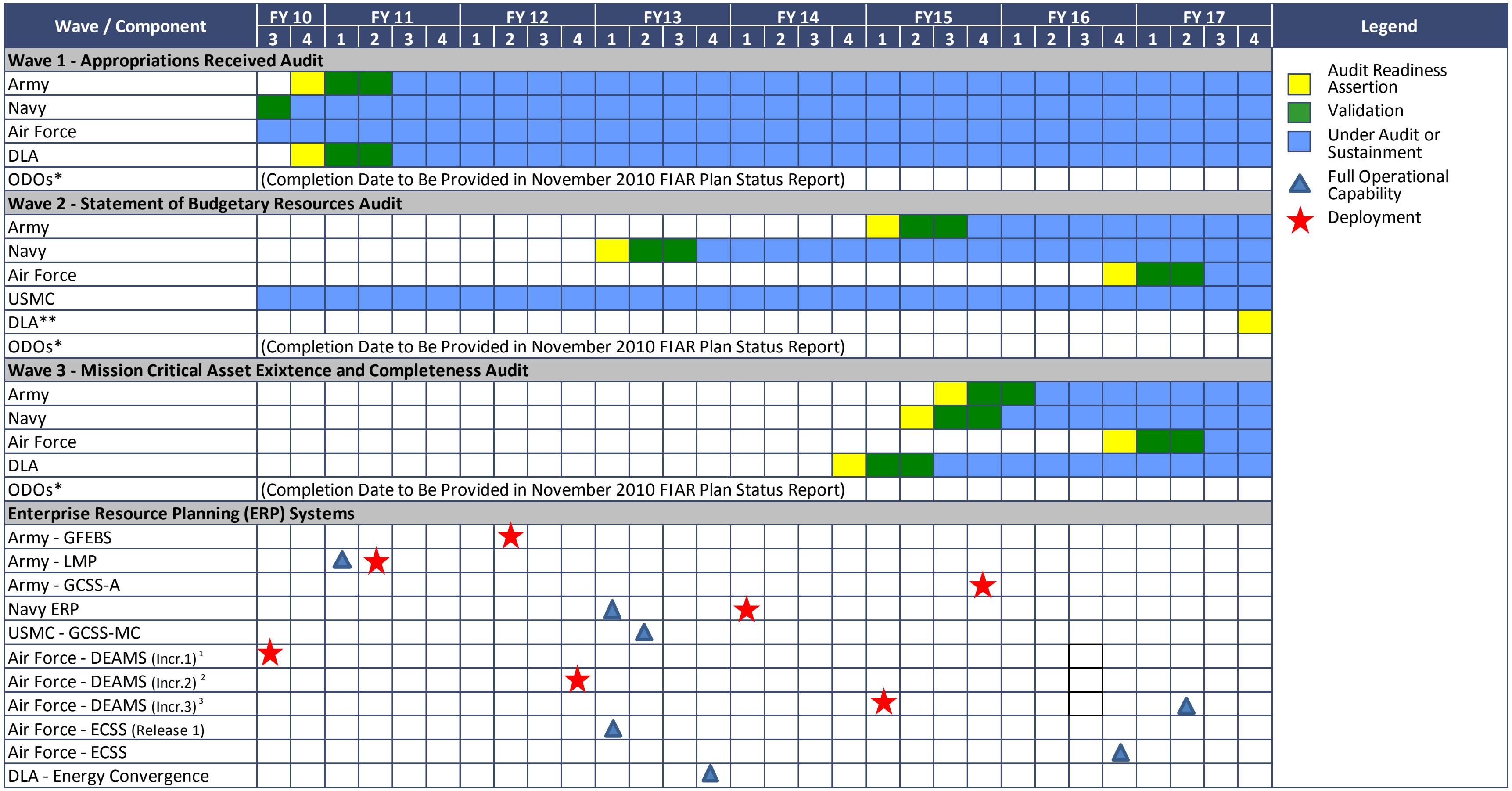
The DoD Audit Advisory Committee, established under the provisions of the Federal Advisory Committee Act of 1972, provides the Secretary of Defense, through the USD(C), independent advice and recommendations on DoD financial management, to include financial reporting processes, internal controls, audit processes, and processes for monitoring compliance with relevant laws and regulations. The Committee is comprised of five members, who are distinguished members of the audit, accounting and financial communities. The members are not DoD employees.

INTERIM AND LONG-TERM MILESTONES

The Department is closely monitoring and tracking audit readiness progress. As shown in Figure I-6, the Navy and Air Force have asserted audit readiness for Wave 1 (Appropriations Received). The OIG validated the Air Force's assertion in FY 2008. The Army and Defense Logistics Agency (DLA) will be audit ready as of the fourth quarter of this fiscal year. Also as shown in Figure I-6 for Wave 2 (SBR Audit), the Army is planning to assert audit readiness for the SBR in the first quarter of FY 2015. The Navy is planning to assert SBR audit readiness in the first quarter of FY 2013. The Air Force is planning to assert audit readiness for the SBR in the fourth quarter of FY 2016, and DLA's plan reflects the fourth quarter of FY 2017 pending completion of the Evaluation and Discovery phase of its end-to-end business processes.

Other than DLA, Figure I-6 does not reflect the plans of any other Defense Agencies or organizations. The Department has analyzed the composition of the DoD Combined SBR to determine all Defense Agencies and other DoD organizations that materially impact the SBR and has begun working with many of them to achieve the objectives of Wave 2. However, at the time of this Report, the other Defense Agencies and organizations do not have FIPs that conform to the FIAR

Figure I-6. Audit Readiness Wave and ERP Milestones



** ODOs are other Defense organizations comprising the remainder of DoD material reporting entities.*

*** DLA's plan reflects the fourth quarter of FY 2017 pending completion of the Discovery phase of its end-to-end business processes.*

1 DEAMS Increment 1 - Implementation at Scott AFB including 2 GSUs (full functionality)

2 DEAMS Increment 2 - Roll-out to USTC, MSC, SDDC, AMC, ACC, USAFE, PACAP, AFSOC, AETC and AFRC

3 DEAMS Increment 3 - Roll-out to AFSPC and AFMC

Note: Wave 3 dates are based on achieving Existence and Completeness audit readiness for all mission critical assets.

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

In Wave 2, the Army, Navy and Air Force are focusing on the General Fund SBR, while DLA on both General Fund and Working Capital Fund. Wave 2 is being worked incrementally by SBR lines and business processes, referred to as assessable units. Their incremental progress and interim milestones (defined as progress that can be accomplished by the end of FY 2012) are reflected in Figure I-7. As indicated, the Components are in the process of both working these assessable units, as well as developing improvement plans for the remaining portions of their SBR. Such is the case for the Army who, as of the date of this Report, has not developed assessable unit plans reflecting achievement of audit readiness prior to the close of FY 2012.

Figure I-6 and Figure I-7 also provide the current status and plans for improving important information on the Department's mission critical assets through existence and completeness audits (Wave 3). Mission critical assets include Military and General Equipment, Real Property, Inventory, and OM&S. Ensuring that the Department's systems contain

Figure I-7. Interim Audit Readiness Goals and Milestones

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

Legend:
- Audit Readiness Assertion
- Validation
- Under Audit or Sustainment
- Capability to Reconcile

accurate and reliable information on these assets is the goal (assets recorded exist and the records are complete). The milestone dates for Wave 3 in Figure I-6 reflect when audit readiness is achieved for the last mission critical asset category (e.g., OM&S in the Army). As part of Wave 3, other important information will be tested and validated, such as the condition of the asset and its location. The objectives and challenges of this wave are presented in section IV of this Report.

Just as with Wave 2, the Components have made significant progress in developing work plans and beginning the work for Wave 3. As shown in Figure I-7, the Army's first assessable units for Military Equipment will be audit ready in the second quarter of FY 2011. All of the Navy's most significant Military Equipment (i.e., aircraft, ships, ICBMs and satellites) will be audit ready by the end of this fiscal year. The Air Force's Military Equipment will be audit ready in the first quarter of FY 2011. In addition, the Air Force will make incremental progress on important assessable units of OM&S (e.g., missile motors, cruise missiles and drones) during FY 2011.

The Department plans to seek validation of its progress through independent examinations, starting with an examination of the Wave 1 efforts on Appropriations Received. If the examinations result in an unqualified opinion of the audit readiness assertion, auditors will be engaged to commence annual audits. The November 2010 FIAR Plan Status Report will more fully describe these examinations.

ACHIEVING FULL AUDITABILITY

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

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

Other concurrent improvement activity, such as the deployment of the ERPs, also supports achieving full auditability. The Department intends to ensure successful ERP implementation, because they are critically needed for business purposes, as well as financial improvement and auditability.

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

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

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

II. FY 2010 NDAA Required Information

The NDAA for Fiscal Year (FY) 2010 directed the Department to prepare a report semi-annually on the status of the implementation of the FIAR Plan and to deliver it to the Congressional Defense Committees not later than May 15 and November 15. The NDAA for FY 2010 also requires the Department to provide in the FIAR Plan Status Report the actions taken and actions planned to address specific issues.

As required, this section provides the Department's actions and plans to:

1. Develop standardized guidance for Component Financial Improvement Plans.
2. Establish a baseline of financial management capabilities and weaknesses at the Component level.
3. Provide results-oriented metrics for measuring and reporting quantifiable results toward addressing financial management deficiencies.
4. Define the oversight roles of the Chief Management Officer (CMO) of the Department and CMOs of the Military Departments and other elements of the Department to ensure the requirements of the FIAR Plan are carried out.
5. Assign accountability for carrying out specific elements of the FIAR Plan to the appropriate officials and organizations at the Component level.
6. Develop mechanisms to track budgets and expenditures for the implementation of the requirements of the FIAR Plan.
7. Develop a mechanism to conduct audits of the military intelligence programs and agencies and to submit their financial statements to the Congress.

Figure II-1 provides a summary of the Department's status on these issues. More detailed information on each of the issues is provided in Appendix 2.

Figure II-1. Summary Table of Issues and Status of Actions Taken and Planned

	Issue	Status	Actions Taken and Planned
1	Develop standardized guidance	Complete	• Standardized guidance issued to the Components during third quarter 2010.
2	Establish financial management capabilities and weaknesses baselines	Started	• Completed the identification of the financial management capabilities to be baselined and developed mechanism to collect baseline status information. • Established a baseline for priority assessable units. • Baseline to be extended beyond initial assessable units.
3	Develop results-oriented metrics	Complete	• Implemented two types of results oriented-metrics. Initial metrics are reported in sections III and IV of this Report.
4	Define oversight roles of DoD CMO and Military Department CMOs	Complete	• Defined CMO oversight roles. • CMO positions are filled and participating in the FIAR process.
5	Assign accountability at Component-level	Complete	• Individuals responsible for corrective actions for the FIAR priorities have been identified in Component Financial Improvement Plans (FIPs).
6	Track FIAR budgets and expenditures	Ongoing	• Component FIPs are required to identify resource requirements and resources committed. • FIAR funding was addressed in a FY 2011 budget process and increased for the Army and Air Force. Navy and DLA had sufficient FIAR funds. • OUSD(C)/Program Budget and FIAR Directorate are tracking FIAR budgets.
7	Develop mechanism for Intelligence Program and Agency audits and financial statements	Complete	• Mechanisms for audits are in place, as demonstrated by FY 2009 opinion on an Intelligence Agency. • Material entities are covered by the FIAR methodology and are or will be included this and future FIAR Plan Status Reports.

III. Audit Ready Statement of Budgetary Resources (Wave 1 & Wave 2)

INTRODUCTION/OVERVIEW

Completion of Wave 1 and Wave 2 result in improving budgetary information and achieving an unqualified audit opinion on the Statement of Budgetary Resources (SBR). Wave 1, Appropriations Received Examination, focuses on one section of the SBR--the Budget Authority section. The Department's immediate focus in Wave 1 and Wave 2 is on General Fund activities, which receive the preponderance of appropriated funds. DLA's Working Capital Fund SBR is also targeted.

Wave 1 is critically important to the Department's overall financial improvement efforts, since it is the first step in receiving, recording and tracking the funds provided to the Department to accomplish its mission. The Navy asserted audit readiness for Appropriations Received in May 2009, and the Office of the Under Secretary of Defense (Comptroller) (OUSD(C)) and Office of the Inspector General (OIG) are in the process of validating their assertion. Air Force Appropriations Received was favorably examined by the OIG in FY 2008. Recognizing the importance of Wave 1, the USD(C) directed the Army and DLA to focus first on Wave 1 and prepare it for examination by the end of FY 2010; and both Components have indicated that they can achieve this goal.

The work to achieve the objective of Wave 1 includes many Defense Agencies (besides DLA), Field Activities and other Defense organizations. The Department is in the process of beginning Wave 1 work with the other Components, and the November 2010 FIAR Plan Status Report will provide the Department's progress.

The Department has dedicated resources to the SBR because it summarizes and reports budgetary information that is widely used to manage operations in the Department. To achieve this priority and achieve a successful audit of the SBR requires the Department to improve the processes, controls and supporting documentation for recording budgetary authority, obligations, outlays and collections.

In addition to focusing on processes, controls and supporting documentation, the Components are also implementing Enterprise Resource Planning (ERP) systems. These ERP systems are designed to correct long-standing challenges with outdated and manually interfaced systems and to provide enterprise-wide visibility into budget execution. With the exception of the Navy and USMC, the ERPs are necessary for the Components to obtain and sustain an unqualified opinion on their SBRs. Each Component is in a different stage of deploying their ERPs.

When Wave 1 and Wave 2 are complete:

- Business and financial processes related to the SBR will have been changed to conform to generally accepted accounting principles (GAAP), and the modernization of essential business and financial systems will be complete;
- Audit evidential matter for SBR transactions will have been evaluated and readily available repositories will be in place to support future audits;
- SBR internal controls will have been documented, tested and strengthened or changed as part of process and system changes, and strong internal control programs will be operational to sustain audit readiness;
- Ability to perform capital and budget planning will improve;
- Business processes and controls will have been documented, controls tested and strengthened, as needed; and
- The Department-wide SBR will be ready for audit. Budgetary information contained in accounting systems of record will be reliable and accurate.

Improvements in all of these areas will not only result in auditable SBRs, but more importantly, will improve the reliability of budget information in various important management reports.

MATERIAL COMPONENTS

The Department is comprised of 3 Military Departments, 18 Defense Agencies, 10 Field Activities and 8 other organizations and 10 Combatant Commands (the "Components"). The financial activity of all of the Components impacts the DoD Consolidated Financial Statements. For some of the Components, their financial activity is immaterial to the overall Department. However, at least 99 percent of the Department's budgetary resources must become audit ready to achieve an unqualified audit opinion on the DoD Combined SBR.

It is important that the Department focus its limited available resources for financial improvement activities on the Components that have the most impact on the DoD Combined SBR. Accordingly, the focus is on the General Fund activities of the Army, Navy and Air Force, as well as the Defense Logistics Agency (DLA), which is predominantly a Working Capital Fund activity. These four Components comprise 66 percent of the Department's budgetary resources.

Nine Defense organizations have 14 percent of the Department's budgetary resources and already have been determined to be audit ready or are presently under audit, such as the U.S. Army Corps of Engineers and U.S. Marine Corps. The remaining 86 percent of the Department's budgetary resources are held by the Military Department's working capital activities and various Defense Agencies, Field Activities and other Defense organizations and funds. See Appendix 3 for a complete listing of all DoD organizations and their respective share of the Department's budgetary resources.

At least 99% of the Department's total budgetary resources are defined as material and must be become audit ready as part of Wave 2.

At the time of this Report, the Department has required Financial Improvement Plans (FIPs) of the Military Departments and DLA to be developed in accordance with the FIAR Strategy and has begun working with the other Defense organizations to achieve 99 percent of DoD budgetary resources. The November 2010 FIAR Plan Status Report will provide additional information on the status and progress of the other Defense organizations efforts to achieve the objectives of Wave 2.

ASSESSABLE UNITS

After the USD(C) directed the Military Departments and DLA to concentrate their financial improvement efforts on the SBR, the first step taken was to analyze and "drill down" into the SBR to determine the business and financial sources (i.e., processes and systems) that produce the reported amounts. The purpose of the drill down was to categorize them into areas (referred to as "assessable units") for organizing their FIPs and for monitoring and reporting progress.

The Components have flexibility to determine their appropriate assessable units based on their differing missions and business operations. However, the Department also has established a core set of standard assessable units that are applicable to all of the Components. In some instances, the Components have decomposed the standard assessable units into lower levels based on a number of factors that include organizational structure (e.g., Commands), business processes or systems. The following are example assessable units:

- Reimbursable Authority
- Civilian Pay
- Military Pay
- Contracts
- Military Standard Requisitioning and Issue Procedures (MILSTRIP) Orders
- Reimbursable Work Orders

- Transportation of People
- Fund Balance with Treasury (FBWT).

In the sections that follow, the Components' status and progress is reported by the above assessable units, where financial improvement activity has started.

AUDIT READINESS DEFINED

To achieve audit readiness for the SBR, the Components must:

- Design and implement control activities to limit the risk of material misstatements by meeting Key Control Objectives (KCOs), and
- Support account balances with sufficient and competent audit evidence, Key Supporting Documentation (KSD).

To maximize the efficiency and effectiveness of audit readiness efforts, the Department identified standard financial statement assertion risks, KCOs and KSDs required to substantiate transactions and balances by major section of the SBR. The KCOs were obtained from the GAO Financial Audit Manual.

The Components are identifying existing control activities for meeting the KCOs, as well as assessing the quality and availability of supporting documentation needed to assert audit readiness. KCOs are discussed in Appendix 1 of this Report and a complete listing of the KCOs can be found in the DoD FIAR Guidance document located at http://comptroller.defense.gov/FIAR/index.html.

The FIAR guidance, which is being followed by the Components and reflected in their FIPs, provides the methodology (i.e., phases, key tasks, detailed activities, and work products) for achieving audit readiness for the SBR.

COMMON CHALLENGES

Each wave has certain accounting and auditing challenges that must be resolved for the Components to become audit ready. For example, during Wave 2 the Components must address beginning balances for FBWT and SBR line items. Additionally, each Component engages in financial transactions with other Components through the use of Military Interdepartmental Purchase Requests (MIPRs). These agreements may result in reimbursable agreements with or without advance or may result in direct-cite of Component funding. These types of financial transactions increase risks associated with the recording of obligations. Typically, obligations are recorded when the service provider signs the agreement. If the performing organization does not sign the document before the end of the year, obligations may be incurred and not recorded in the proper period.

Accounts Payable accruals also affect the amounts reported in the SBR. The Components must design effective accrual processes to ensure that goods or services received, but not billed, are properly accounted for in the SBR.

Other common challenges include:

- FBWT must be remediated at the same time as other major line items (e.g., Accounts Receivable and Accounts Payable) to support unobligated balances available and unavailable, and cash collections and outlays. This includes supporting at least five years of past activity.
- An audit of Accounts Receivable (including Unfilled Customer Orders) and Accounts Payable (including Undelivered Orders) must support budgetary amounts reported on the SBR.
- Reconciling Defense Agencies' FBWT because they share one Treasury account.
- Obtaining Service Provider Statements on Auditing Standards (SAS) No. 70 internal control audits for the processes and systems they use in supporting their DoD customers. Where deficiencies are identified, compensating controls must be designed and implemented.

AUDIT READINESS CAPABILITY BASELINE, STATUS AND PLANS

This section of the Report provides a summary-level view of the status and plans of the Army, Navy, Air Force and DLA to achieve Wave 1 and Wave 2 audit readiness. The information is presented in three different figures per Component, as follows:

1. Audit Readiness Plans
2. Key Control Objective (KCO) Status and Projections
3. Key Supporting Documentation (KSD) Status and Projections

In addition to identifying the planned completion of audit readiness milestones (i.e., Audit Readiness Assertion, Validation, and Under Audit or Sustainment), the Audit Readiness Plans include the planned completion of the following Success Criteria/Key Capabilities:

1. Implement FBWT reconciliation capability,
2. Controls over recording obligations are effective,
3. Controls over recording receipt of goods and services are effective,
4. Controls over recording disbursements are effective, and
5. Supporting documentation is retained and available to meet audit requests.

The status, as presented in the KCO and KSD figures, represents each Component's financial management capability baseline--that is, the effectiveness of their internal controls and ability to readily provide evidential matter to auditors as of the date of this Report. Over time, as the Components execute their FIPs, these tables and charts will measure their progress from the baseline (of March 31, 2010) to achieving audit readiness.

The KCO and KSD metrics track progress in achieving the end-state outcome of auditability. The KCO metrics reflect the Components' progress in achieving a strong internal control program that ensures financial transactions are timely and accurately recorded.

The KCO metrics provide management with visibility of the Components' assessment, testing and remediation activity until the KCOs have been determined to be effective. A standard set of KCOs are embedded in each of the Components' FIPs and have been linked to the discovery and corrective activities that identify them as either effective or a weakness.

KSD metrics capture the Components' progress in identifying supporting documentation deficiencies and problems that must be remediated before achieving auditability. Maintaining and making readily available acceptable evidential matter is critical to successful audits. This has been a long-standing deficiency in the Department and resolving it is essential. The FIAR methodology provides guidance to assist in resolving this impediment, and this metric tracks progress.

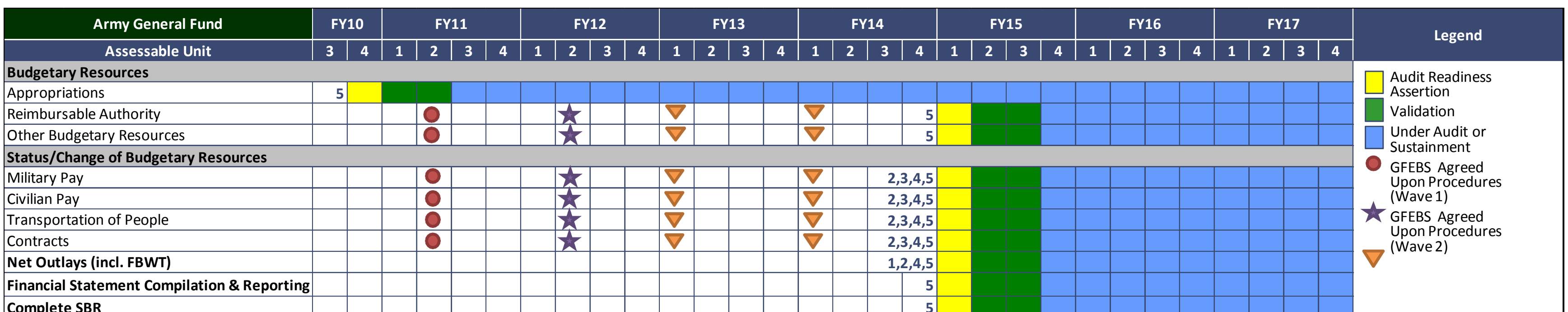
It is important to note that most of the reported status in the KCO and KSD figures that follow reflect zero percent (0%) assessed and zero percent effective. This means that, at the time of this Report, the Component FIPs did not reflect the outcome of such activity. The Components are in the process of updating their FIPs to reflect this activity, and the November 2010 FIAR Plan Status Report will present an updated status.

Each Component section contains a summary table highlighting its strategy and information pertaining to Wave 1 and Wave 2, as well as other information impacting the Component's approach, challenges or progress.

ARMY

Army	Highlights
Wave 2 Strategy	• Army will achieve SBR audit readiness through the controls implemented in the course of deployment of their ERP (General Fund Enterprise Business System (GFEBS)). • Army has begun testing of controls and source documentation at Army locations with significant amounts of budgetary resources. This testing will identify any issues remaining after implementation of GFEBS. • DFAS is working with the Army to evaluate and address process deficiencies and strengthen controls. • Army Audit Agency is also a key partner providing support and staff for the Army plan.
Figure III-1. Audit Readiness Plans	• Wave 1 - Appropriations Received: Audit ready in fourth quarter of FY 2010. • Wave 2 - SBR: Audit ready in first quarter of FY 2015.
Figure III-2. KCO Status and Projections	• 12% of the KCOs have been assessed and no KCOs have been determined to be effective.
Figure III-3. KSD Status and Projections	• No KSDs have been assessed.

Figure III-1. Audit Readiness Plans



Success Criteria / Key Capability

1 Implement FBWT reconciliation capability
2 Controls over recording obligations are effective
3 Controls over recording receipt of goods or services are effective
4 Controls over recording disbursements are effective
5 Supporting documentation is retained and available to meet audit standards

Blank rows indicate either no FIP submitted or no assertion date given for an assessable unit.

Note 1: "Transportation of People" is an aggregate of Obs Travel PCS, Obs Travel TDY

Note 2: "Financial Statement Compilation and Reporting" is an aggregate of Departmental Reporting and Pre-Departmental Reporting

Figure III-2. SBR Key Control Objective (KCO) Status and Projections

Army Assessable Unit	# KCOs	% Assessed	% Effective
SBR	**77**	**12%**	**0%**
Financial Statement Compilation & Reporting	**6**	**0%**	**0%**
Budgetary Resources	**17**	**0%**	**0%**
Appropriations	4	0%	0%
Reimbursable Authority	5	0%	0%
Other Budgetary Resources	8	0%	0%
Status/Change of Budgetary Resources	**24**	**0%**	**0%**
Military Pay	24	0%	0%
Civilian Pay	24	0%	0%
Transportation of People	24	0%	0%
Contracts	24	0%	0%
Net Outlays (incl. FBWT)	**30**	**30%**	**0%**

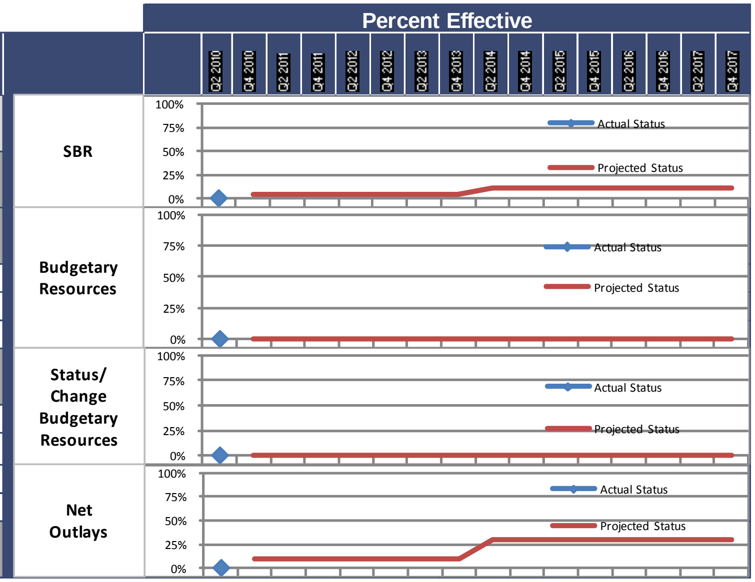
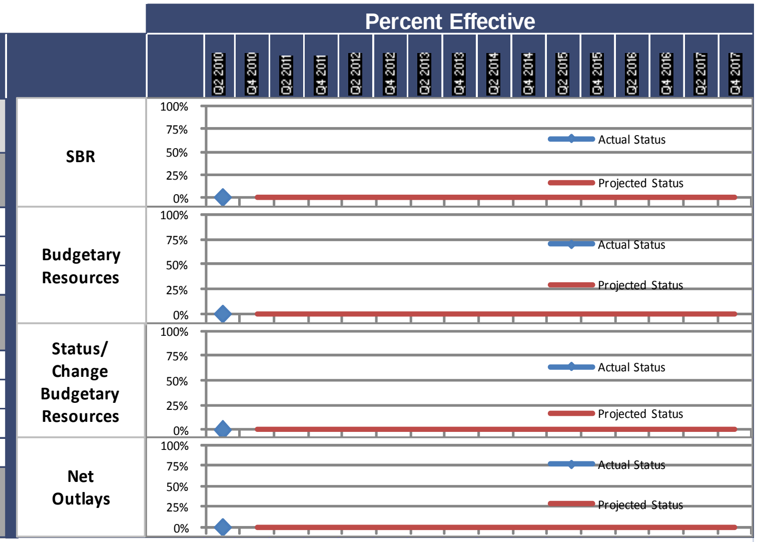


Figure III-3. SBR Key Supporting Document (KSD) Status and Projections

Army Assessable Unit	# KSDs	% Assessed	% Effective
SBR	**64**	**0%**	**0%**
Budgetary Resources	**36**	**0%**	**0%**
Appropriations	16	0%	0%
Reimbursable Authority	17	0%	0%
Other Budgetary Resources	17	0%	0%
Status/Change of Budgetary Resources	**7**	**0%**	**0%**
Military Pay	7	0%	0%
Civilian Pay	7	0%	0%
Transportation of People	7	0%	0%
Contracts	7	0%	0%
Net Outlays (incl. FBWT)	**21**	**0%**	**0%**

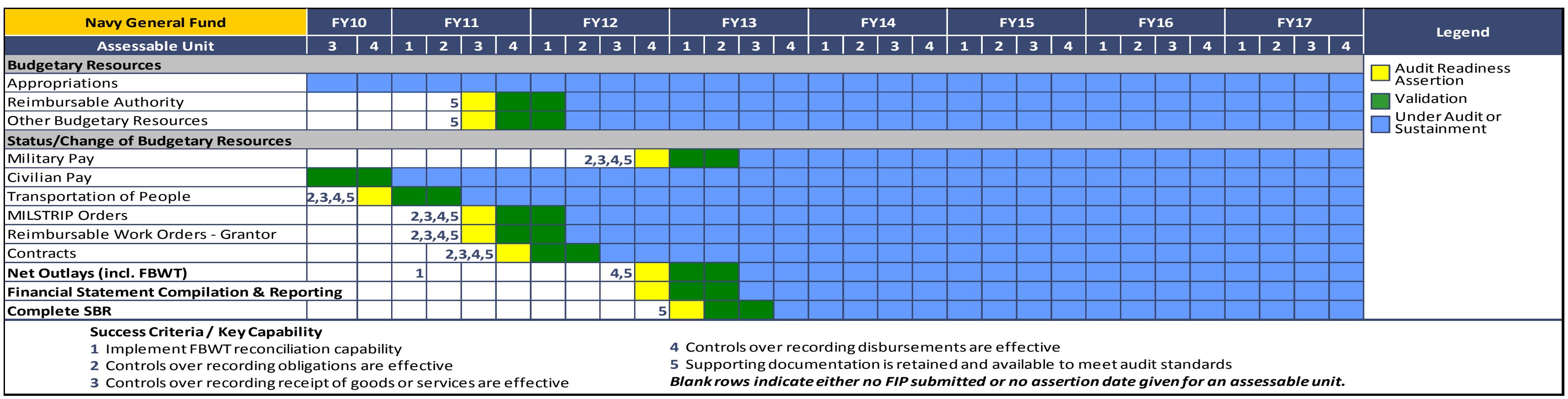


NOTE: In Wave 2, there are 8 KSDs related to Internal Controls. For purposes of metrics reporting, these are only counted once and are included in the Other Budgetary Resources line above. However, these KSDs will need to be addressed for all assessable units.

NAVY

Navy	Highlights
Wave 2 Strategy	• Defined audit readiness as the completion of three SBR-focused audit readiness efforts: o Assertion of business process segments through the verification of design and operating effectiveness of internal controls, o Documentation of the financial compilation process, and o Substantive testing and analysis. • Audit readiness is not dependent on the full deployment of Navy ERP. Rather, SBR auditability will be achieved in the legacy and ERP environment.
Figure III-4. Audit Readiness Plans	• Wave 1 - Appropriations Received: Audit ready in fourth quarter of FY 2009. • Wave 2 - SBR: Audit ready in first quarter of FY 2013.
Figure III-5 KCO Status and Projections	• 23% of the KCOs have been assessed and 4% have been determined to be effective.
Figure III-6. KSD Status and Projections	• 58% of KSDs have been assessed and 27% have been determined to be effective.

Figure III-4. Audit Readiness Plans



Notes: 1: Reimbursable Authority = RWOP 2: Utilities AU will be reported under the Contract AU 3: Appropriations became assertion-ready prior to the development of the KCOs and FIAR Guidance
4: In Wave 2, there are 3 KCOs related to Financial Reporting and 8 KSDs related to Internal Controls. For purposes of metrics reporting, these are only counted once and are included in the Other Budgetary Resources line above. However, these KCOs and KSDs will need to be addressed for all assessable units.

Figure III-5. SBR Key Control Objective (KCO) Status and Projections

Navy Assessable Unit	# KCOs	% Assessed	% Effective
SBR	**77**	**23%**	**4%**
Financial Statement Compilation & Reporting	**6**	**0%**	**0%**
Budgetary Resources	**17**	**24%**	**18%**
Appropriations	4	100%	75%
Reimbursable Authority	5	0%	0%
Other Budgetary Resources	8	0%	0%
Status/Change of Budgetary Resources	**34**	**0%**	**0%**
Civilian Pay	34	50%	50%
Military Pay	34	0%	0%
Contracts	34	0%	0%
MILSTRIP Orders	34	0%	0%
Reimbursable Work Orders	34	0%	0%
Transportation of People	34	0%	0%
Net Outlays (Incl. FBWT)	**20**	**70%**	**0%**

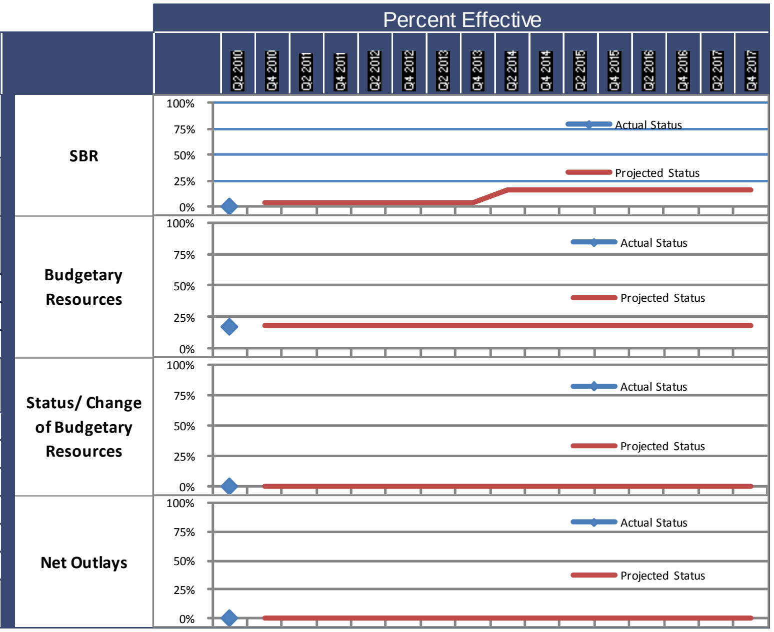
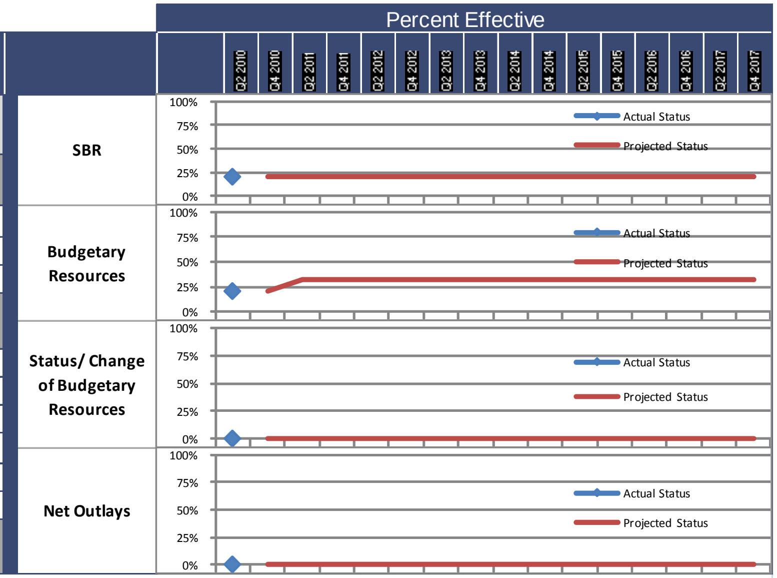


Figure III-6. SBR Key Supporting Document (KSD) Status and Projections

Navy Assessable Unit	# KSDs	% Assessed	% Effective
SBR	**64**	**58%**	**27%**
Budgetary Resources	**50**	**32%**	**32%**
Appropriations	16	100%	100%
Reimbursable Authority	17	0%	0%
Other Budgetary Resources	17	0%	0%
Status/Change of Budgetary Resources	**7**	**0%**	**0%**
Civilian Pay	7	14%	14%
Military Pay	7	0%	0%
Contracts	7	0%	0%
MILSTRIP Orders	7	0%	0%
Reimbursable Work Orders	7	0%	0%
Transportation of People	7	0%	0%
Net Outlays (Incl. FBWT)	**21**	**95%**	**0%**

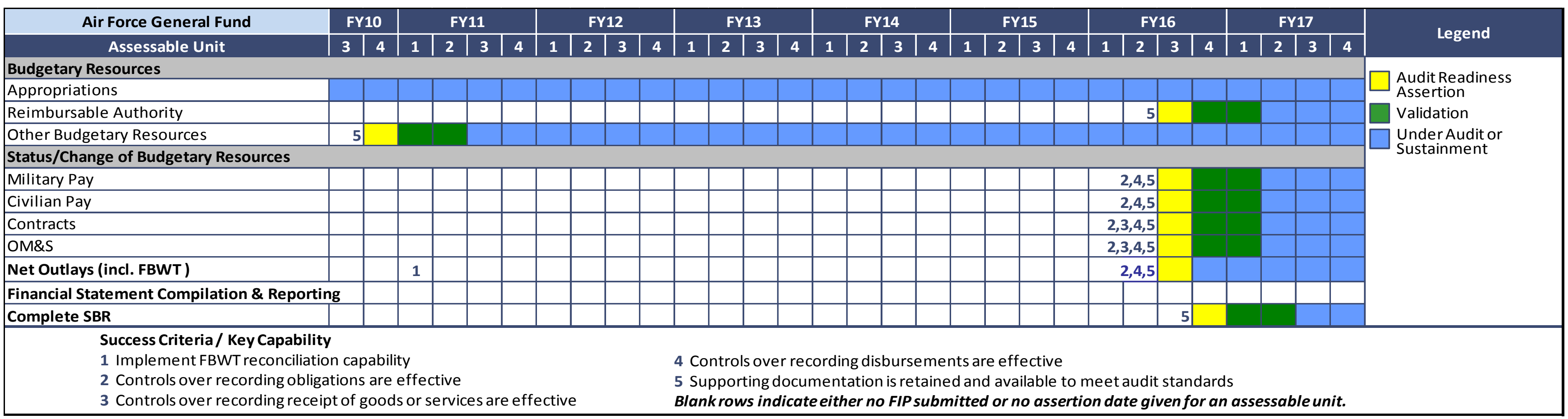


Note 1: In Wave 2, there are 8 KSDs related to Internal Controls. For purposes of metrics reporting, these are only counted once and are included in the Other Budgetary Resources line above. However, these KSDs will need to be addressed for all assessable units.

AIR FORCE

Air Force	Highlights
Wave 2 Strategy	• Current efforts focus on the Budgetary Resources section of the SBR and FBWT reconciliation. • Additional resources in FY 2011 will enable work to begin on other SBR areas. • SBR audit readiness is dependent on the deployment of the Defense Enterprise Accounting Management System (DEAMS) and Expeditionary Combat Support System (ECSS) ERPs.
Figure III-7. Audit Readiness Plans	• Wave 1 - Appropriations Received and Non-Expenditure Transfers: Successfully audited by the DoD IG in FY 2008. • Wave 2 - SBR: Audit ready in fourth quarter of FY 2016.
Figure III-8. KCO Status and Projections	• 92% of KCOs have been assessed and 6% are effective.
Figure III-9. KSD Status and Projections	• 56% of KSDs have been assessed and 28% are effective.

Figure III-7. Audit Readiness Plans



Note 1: "Contracts" is an agreggation of ME Equipment, Real Property, Other Assets, Non-A2R

Note 2: Non-expenditure Transfers is included in the Other Budgetary Resources Line

Figure III-8. SBR Key Control Objective (KCO) Status and Projections

Air Force Assessable Unit	# KCOs	% Assessed	% Effective
SBR	**77**	**92%**	**6%**
Financial Statement Compilation & Reporting	**6**	**0%**	**0%**
Budgetary Resources	**17**	**100%**	**100%**
Appropriations	4	100%	100%
Reimbursable Authority	5	100%	0%
Other Budgetary Resources	8	100%	0%
Status/Change of Budgetary Resources	**34**	**100%**	**0%**
Military Pay	34	100%	0%
Civilian Pay	34	100%	0%
Contracts	34	100%	0%
OM&S	34	100%	0%
Net Outlays (incl. FBWT)	**20**	**100%**	**5%**

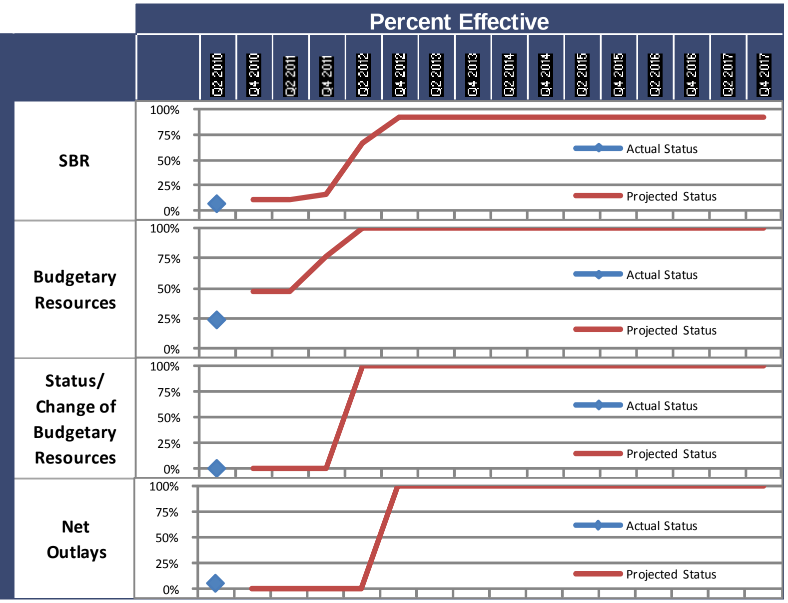
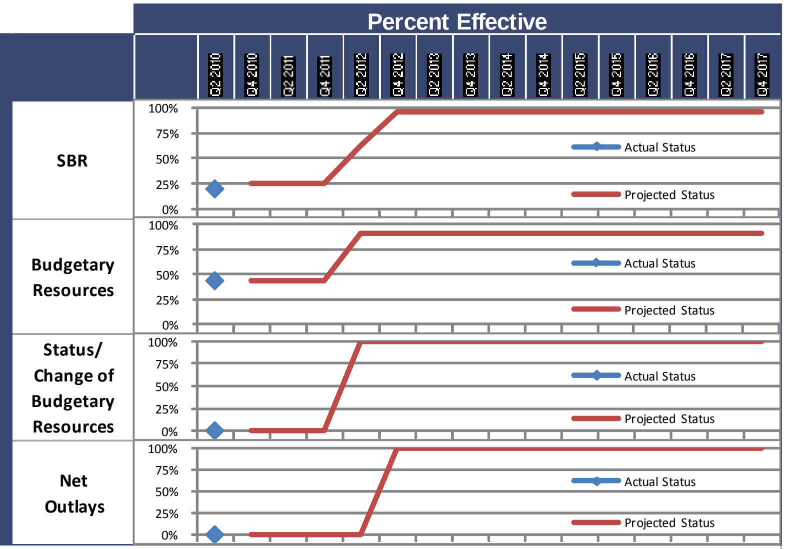


Figure III-9. SBR Key Supporting Document (KSD) Status and Projections

Air Force Assessable Unit	# KSDs	% Assessed	% Effective
SBR	**64**	**56%**	**28%**
Budgetary Resources	**36**	**100%**	**50%**
Appropriations	16	100%	100%
Reimbursable Authority	17	100%	0%
Other Budgetary Resources	17	100%	12%
Status/Change of Budgetary Resources	**7**	**100%**	**0%**
Military Pay	7	100%	0%
Civilian Pay	7	100%	0%
Contracts	7	100%	0%
OM&S	7	100%	0%
Net Outlays (incl. FBWT)	**21**	**100%**	**0%**



**NOTE: In Wave 2, there are 8 KSDs related to Internal Controls. For purposes of metrics reporting, these are only counted once and are included in the Other Budgetary Resources line above. However, these KSDs will need to be addressed for all assessable units.*

DLA

DLA	Highlights
Wave 2 Strategy	• Improvement work is organized by end-to-end business process: Budget to Report, Procure to Pay, Order to Cash, Record to Report, and Hire to Retire. • ERP (Enterprise Business System (EBS)) has been deployed, except for Energy business line. Improvements to EBS reporting are needed to achieve audit readiness. • DLA is working with DFAS to obtain documentation on business processes and flow charts that identify DFAS internal controls. DFAS will be performing and reporting on their internal control testing. DLA is linking DFAS processes to DLA's end-to-end business cycles. • DLA is part of Treasury Index 97 appropriation and shares that appropriation with many other Defense Agencies. DLA's FBWT balances reported on financial statements are determined by DFAS-IN using the Cash Management Report (CMR) process. The CMR process is currently under audit by the DoD IG, and DLA is awaiting the outcome of the audit to determine next steps.
Figure III-10. Audit Readiness Plans	• Wave 1 - Appropriations Received audit ready in fourth quarter of FY 2010. • Wave 2 - SBR: Audit ready in first quarter of FY 2017, pending completion of the Evaluation and Discovery phase.
Figure III-11. KCO Status and Projections	• 14% of the KCOs have been assessed across all applicable assessable units. No KCOs are effective.
Figure III-12 KSD Status and Projections	• No KSDs have been assessed.

Figure III-10. Audit Readiness Plans

DLA	FY10		FY11				FY12				FY13				FY14				FY15				FY16				FY17			
Assessable Unit	**3**	**4**	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**	**1**	**2**	**3**	**4**
Wave 1 - Budgetary Resources - Appropriations																														
Budget to Execute	5																													
Record to Report	5																													
Wave 2 - Remaining Statement of Budgetary Resources Line-items																														
Budget to Execute																													5	
FBWT					1				2,4,5,6																					
Hire to Retire																													2,3,4,5	
Order to Cash																													3,4,5,6	
Procure to Pay																													2,3,4,5	
Record to Report																													2,3,4,5	
Complete SBR																													5	

Legend
- Audit Readiness Assertion
- Validation
- Under Audit or Sustainment

Success Criteria / Key Capability
1 Implement FBWT reconciliation capability
2 Controls over recording obligations are effective
3 Controls over recording receipt of goods or services are effective
4 Controls over recording disbursements are effective
5 Supporting documentation is retained and available to meet audit standards
6 Controls over recording collections are effective

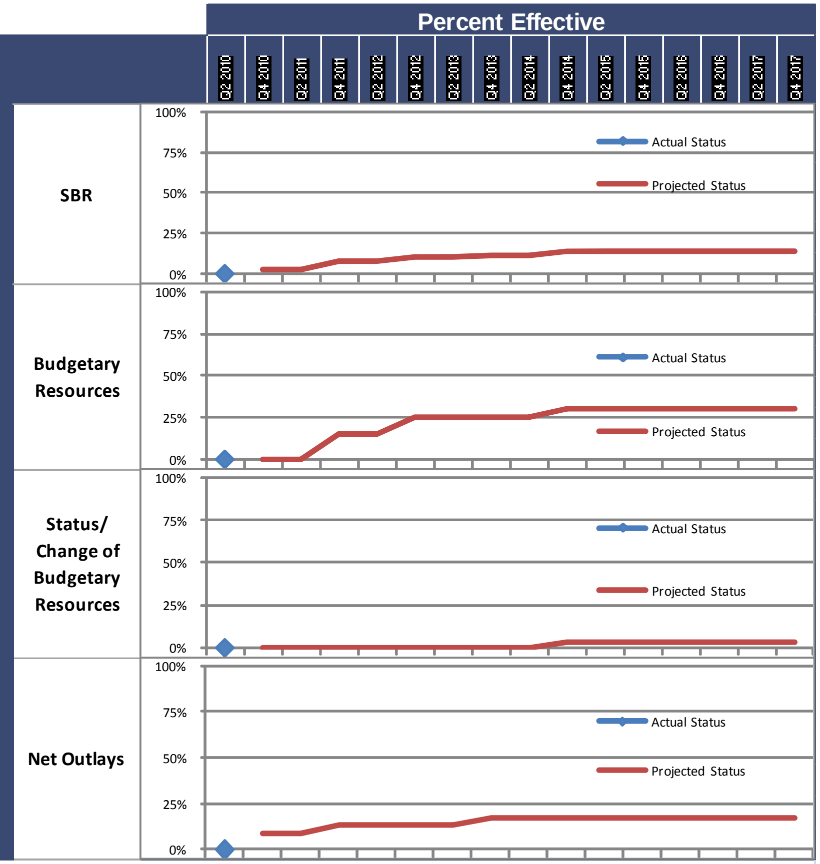
Blank rows indicate either no FIP submitted or no assertion date given for an assessable unit.

Note 1: Wave 1 Appropriations is a subset of the Budget to Execute

Note 2: Financial Statement Compilation & Reporting is an aggregate of the Record to Report

Figure III-11. SBR Key Control Objective (KCO) Status and Projections

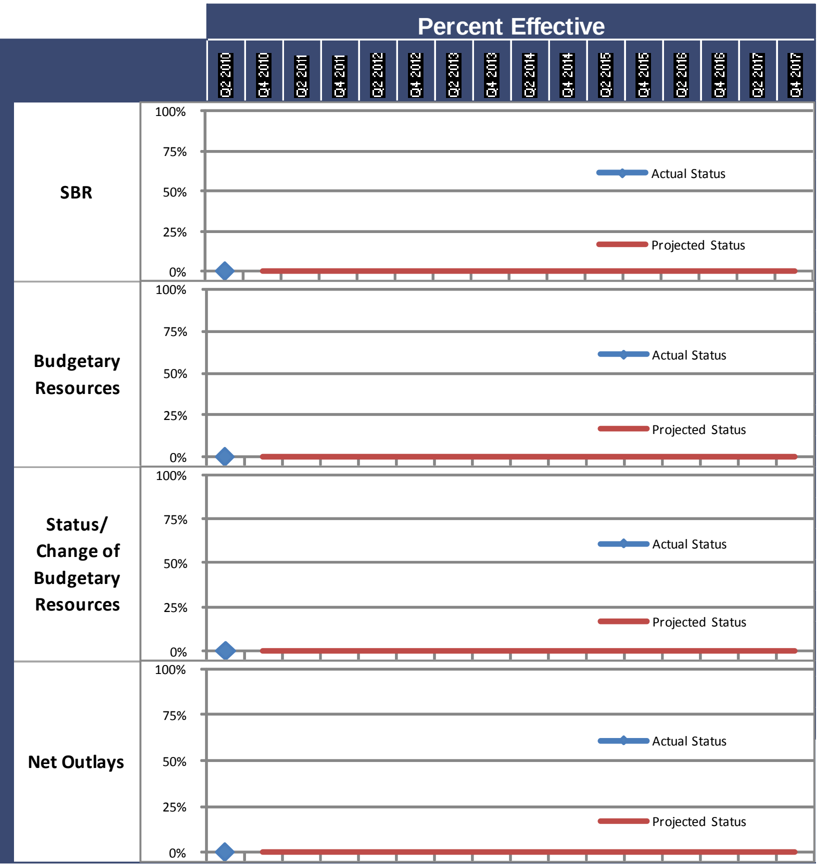
DLA Assessable Unit	# KCOs	% Assessed	% Effective
SBR	**77**	**14%**	**0%**
Budgetary Resources	**20**	**30%**	**0%**
Budget to Execute	15	67%	0%
FBWT	2	0%	0%
Hire to Retire	5	0%	0%
Order to Cash	3	67%	0%
Procure to Pay	2	0%	0%
Record to Report	5	60%	0%
Status/Change of Budgetary Resources	**34**	**3%**	**0%**
Budget to Execute	5	0%	0%
Hire to Retire	29	0%	0%
Order to Cash	12	17%	0%
Procure to Pay	32	34%	0%
Record to Report	2	0%	0%
Net Outlays (incl. FBWT)	**23**	**17%**	**0%**
Budget to Execute	3	0%	0%
FBWT	16	19%	0%
Hire to Retire	7	0%	0%
Order to Cash	10	70%	0%
Procure to Pay	9	78%	0%
Record to Report	5	100%	0%



Note: Certain KCOs apply to multiple sections of the SBR and for the purposes of this metric, they are represented multiple times. As a result, the total KCOs within all sections of the SBR exceeds the total 77 KCOs.

Figure III-12. SBR Key Supporting Document (KSD) Status and Projections

DLA Assessable Unit	# KSDs	% Assessed	% Effective
SBR	**64**	**0%**	**0%**
Budgetary Resources	**36**	**0%**	**0%**
Budget to Execute	26	0%	0%
FBWT	0	0%	0%
Hire to Retire	12	0%	0%
Order to Cash	12	0%	0%
Procure to Pay	12	0%	0%
Record to Report	12	0%	0%
Status/Change of Budgetary Resources	**7**	**0%**	**0%**
Budget to Execute	0	0%	0%
Hire to Retire	7	0%	0%
Order to Cash	7	0%	0%
Procure to Pay	7	0%	0%
Record to Report	7	0%	0%
Net Outlays (incl. FBWT)	**21**	**0%**	**0%**
Budget to Execute	0	0%	0%
FBWT	13	0%	0%
Hire to Retire	8	0%	0%
Order to Cash	8	0%	0%
Procure to Pay	8	0%	0%
Record to Report	8	0%	0%



PROGRESS METRICS

Results-oriented, progress metrics provide a useful means for management to monitor and measure financial improvement progress. This section of the Report provides two types of metrics:

- Metrics that measure progress by validations and audits, and
- Metrics that measure progress by improvements to financial operations.

Progress Measured by Validations and Audits

Figure III-13 provides the Department's current status and interim goals--to be accomplished by the end of FY 2012--for achieving the Wave 1 and Wave 2 objectives, as well as achieving auditability of the Fund Balance with Treasury (FBWT) line of the Balance Sheet. Achieving FBWT audit readiness is essential to preparing for an SBR audits.

As shown in Figure III-13, 80 percent of the Appropriations Received line of the SBR will be validated through independent examinations as audit ready in FY 2011, and 14 percent of the DoD Combined SBR will be validated as audit ready in FY 2011. These percentages may change for FY 2012 as the Department begins working with the Other Defense Organizations (ODOs) not now included in the FIAR Plan. The November 2010 FIAR Plan Status Report will provide updated information on the status and progress of the ODOs. The percentages are based on the total reported amounts on the Department's FY 2008 financial statements. The percentage increase for SBR Audit Ready from FY 2009 to FY 2010 is for the audit of the USMC SBR.

Figure III-13 SBR Priority Status and Interim Goals

	FY 2009	FY 2010	FY 2011	FY 2012
SBR Appropriations Received Audit Ready	38%	53%	80%	80%
SBR Audit Ready	13%	14%	14%	14%
FBWT Audit Ready	7%	8%	30%	30%

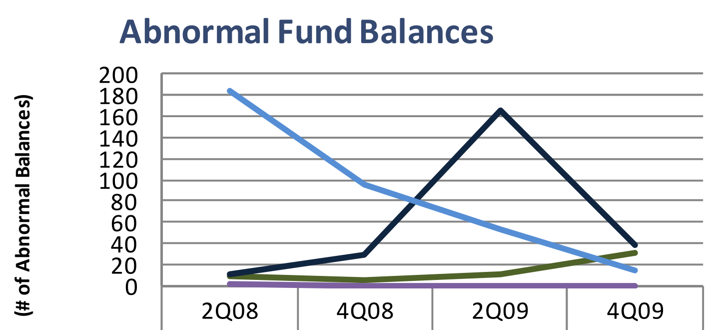
Progress Measured by Improvements to Financial Operations

The second type of metric has a direct relationship to budgetary information and the SBR and measures improvements to financial operations. The metrics either measure outcomes of better budgeting information (e.g., Abnormal Fund Balances) or measure progress improvements needed to achieve better budgetary information.

Each metric is accompanied by a description and identifies the goals, benefits and results. These metrics include the following:

- Figure III-14. Abnormal Fund Balances
- Figure III-15. In-Transit Disbursements and Collections Over 60 Days
- Figure III-16. Unmatched Disbursements Over 120 Days
- Figure III-17. Negative Unliquidated Obligations Over 120 Days
- Figure III-18. Appropriations with Negative Balances

Figure III-14.



	2Q08	4Q08	2Q09	4Q09
Army	10	5	11	31
Navy	11	30	165	38
Air Force	184	95	54	15
DLA	1	0	0	0

Metric Title: Abnormal Fund Balances
Wave 2 - SBR

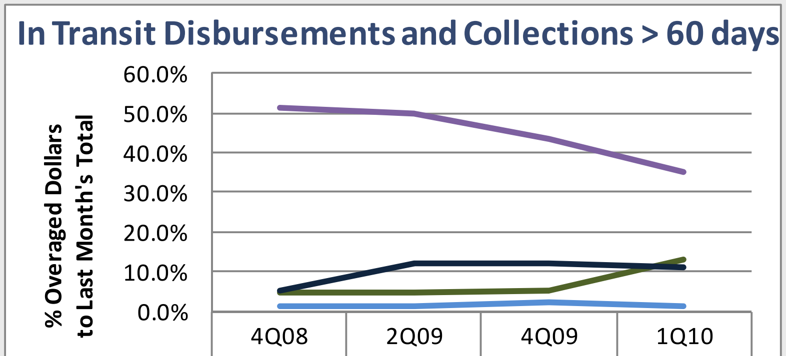
Description:
This metric measures the number of abnormal fund balances, at levels lower than the appropriation level, not resolved within 60 days. An abnormal balance exists when a debit balance account has a credit balance or vice versa.

Goal:
0 abnormal balances unresolved in greater than 60 days.

Benefit:
Preventing and/or timely resolution of abnormal fund balances results in more accurate obligation and outlay balances on management reports and the Statement of Budgetary Resources resulting in better utilization of funds in the year appropriated.

Results:
Air Force and DLA reconciliation efforts are resulting in improved and consistent good results in this metric.

Figure III-15.



	4Q08	2Q09	4Q09	1Q10
Army	4.6%	4.8%	5.4%	12.9%
Navy	5.3%	11.9%	12.0%	11.1%
Air Force	1.2%	1.1%	2.2%	1.5%
DLA	51.5%	49.9%	43.6%	35.0%

Metric Title: In-Transit Disbursements and Collections > 60 days
Wave 2 - SBR

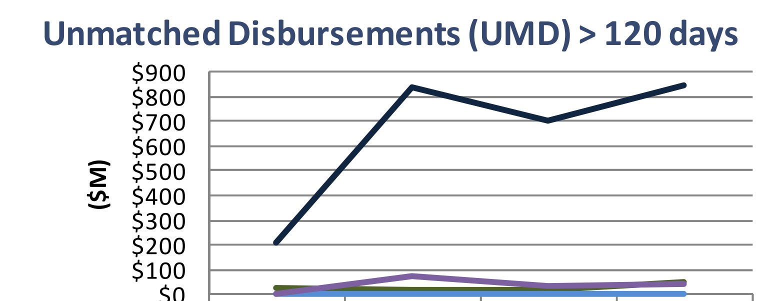
Description:
This metric measures Component timeliness in recording collections and disbursements. An in-transit disbursement or collection is a payment or collection made by one activity on behalf of a another accounting activity, but not yet recorded in the general ledger of the accounting entity.

Goal:
To have 5% or less of the prior month's total absolute in-transit balance greater than 60 days old.

Benefit:
Timely recording of disbursements and collections results in greater accuracy of Components' accounts balances on management reports and the SBR resulting in better utilization of funds.

Results:
Air Force consistently meets the goal. Navy and DLA show improvement; Army on the verge of meeting the the goal at the end of FY09.

Figure III-16.



	4Q08	2Q09	4Q09	1Q10
Army	$28.64	$16.98	$18.62	$46.89
Navy	$205.68	$835.13	$701.01	$845.28
Air Force	$0.44	$0.00	$0.00	$0.00
DLA	$0.00	$70.66	$33.84	$40.43

Metric Title: Unmatched Disbursements (UMD) > 120 days
Wave 2 - SBR

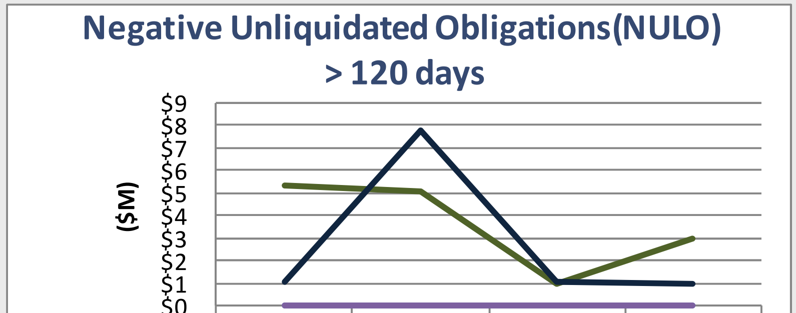
Description:
This metric measures Component success in correcting UMD amounts that are 120 days old or older. A UMD occurs when a disbursement cannot be matched to an obligation in the accounting system.

Goal:
No UMD amounts greater than 120 days old.

Benefit:
Preventing and/or timely resolution of UMDs results in greater accuracy of Components' accounts balances on management reports and the SBR resulting in better utilization of funds.

Results:
Navy's lack of transaction level visibility hinders overaged UMD reductions. Appropriate data matching through automated systems is imperative to overcome UMDs. Overaged UMDs have been considerably reduced from a September 1999 level of $2.03B.

Figure III-17.



	4Q08	2Q09	4Q09	1Q10
Army	$5.36	$5.10	$1.00	$2.99
Navy	$1.10	$7.75	$1.11	$1.00
Air Force	$0.00	$0.00	$0.00	$0.00
DLA	$0.00	$0.00	$0.00	$0.00

Metric Title: Negative Unliquidated Obligations > 120 days
Wave 2 - SBR

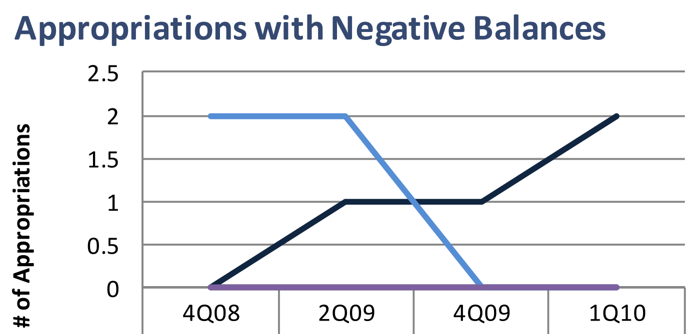
Description:
This metric measures Component payment discrepancies, known as negative unliquidated obligations (NULOs), caused by disbursing amounts greater than the corresponding obligations that are not resolved within 120 days.

Goal:
No NULOs greater than 120 days old.

Benefit:
Preventing and/or timely resolution of NULOs results in greater accuracy of Components' accounts balances on management reports and the SBR resulting in better utilization of funds.

Results:
Overaged NULOs have been considerably reduced from a September 1999 level of $1.6B.

Figure III-18.



	4Q08	2Q09	4Q09	1Q10
Army	0	0	0	0
Navy	0	1	1	2
Air Force	2	2	0	0
DLA	0	0	0	0

Metric Title: Appropriations with Negative Balances
Wave 2 - SBR

Description:
This metric measures the number of appropriations with negative balances not resolved within three months of expenditures exceeding appropriated amounts.

Goal:
No appropriations with negative balances over 3 months old.

Benefit:
Preventing and/or timely resolution of negative appropriation balances results in greater accuracy of Components' accounts balances on management reports and the SBR resulting in better utilization of funds. It also demonstrates proper stewardship of public funds and adherence to appropriation laws and regulations.

Results:
Components continue to meet this goal on a regular basis.

IV. Audit Ready Existence and Completeness of Assets (Wave 3)

INTRODUCTION/OVERVIEW

Successful execution of the Department's military missions depends on a properly equipped and supplied warfighting force. Properly equipping and supplying the forces requires accurate and reliable property, logistics and inventory systems information to manage the mission critical assets. This information includes unique item identifiers (e.g., serial number), quantity, location and condition. In the Department, these systems are often referred to as accountable property systems of record (APSRs) and are typically not operated by the financial community. Much of this information is also important to financial statement audits.

Aware of the importance of this information to decision makers and the warfighter, the USD(C) directed the Components to first focus their improvement efforts on ensuring the key information in the APSRs is accurate and reliable and validated through existence and completeness audits. The USD(C) also directed the Components to place a lower priority on valuing assets until information relating to existence and completeness is successfully audited.

Existence and completeness are two of five management assertions about financial statements. By the existence and completeness assertions, management is asserting that all reported assets exist and that all assets are being reported. Achieving accurate and reliable asset information and validating its accuracy through existence and completeness audits are the objectives of Wave 3. These objectives are also critical steps to achieving successful future financial statement audits.

MISSION CRITICAL ASSETS

For the purposes of Wave 3, mission critical assets include the following types of assets, which is consistent with how they are reported in the notes accompanying the Department's Balance Sheet:

- Military Equipment,
- Real Property,
- Inventory,
- Operating Materials and Supplies (OM&S), and
- General Equipment

MANAGEMENT INFORMATION

In addition to testing the APSRs to determine if assets recorded in the system physically exist and that the system is complete--i.e., includes all assets that meet property accountability requirements, the Department is also having the auditors test important management information maintained in these same systems.

Examples of this information include:

- Unique Identifiers (e.g., item unique identification [IUID] number, Real Property UID [RPUID], aircraft tail number, ship number)
- Location (e.g., military installation/base)
- Condition (e.g., operational status/in-service)
- Accountable organization (e.g., 374th Tactical Airlift Wing)
- Accountable individual (e.g., SSGT John Smith)

Ensuring that this information is accurate and reliable is important not only for managing mission critical assets, but also for proper financial reporting and future financial statement audits. For example, the condition of an asset might indicate that it was taken out of service and no longer should be depreciated.

When Wave 3 is completed, the Department's:

- Information pertaining to the existence and completeness of mission critical assets contained in APSRs will be reliable and accurate,
- Specific important management information (e.g., condition, location) pertaining to mission critical assets will be reliable and accurate,
- Maintenance planning and asset disposition decisions will be improved,
- Ability to perform capital and budget planning will improve, and
- Business and financial processes and controls will have been documented, controls tested and strengthened.

MATERIAL COMPONENTS

The FIAR Plan is predominantly focused on the improvement efforts of the Army, Navy, Air Force and Defense Logistics Agency (DLA), which are the most significant (material) DoD entities with regard to their budgets and appropriations, personnel, assets and liabilities. However, the U.S. Marine Corps (USMC), Special Operations Command (SOCOM) and Missile Defense Agency (MDA) also have material amounts (in dollar value) of military equipment. Accordingly, the objectives of Wave 3 (i.e., accurate and reliable asset information and validating its accuracy through existence and completeness audits) are applicable to the Military Services, DLA, SOCOM and MDA.

Figure IV-1 provides the acquisition values reported to DFAS in the Defense Departmental Reporting System for the mission critical assets of the Military Services, DLA, SOCOM and MDA.

ASSESSABLE UNITS

As shown in Figure IV-1, each Component has a large inventory of mission critical assets, which are located across the United States and deployed to various countries worldwide. This alone makes this objective of Wave 3 challenging, but to complicate it further, many information systems are used within the Components, and many systems are being replaced by modern integrated systems.

Figure IV-1 FY 2009 Asset Acquisition Values

Component	FY 2009 Dollars in Billions				
	Military Equipment	Real Property	Inventory	OM&S	General Equipment
Army	141.2	64.4	23.2	34.5	5.6
Navy	337.3	37.1	11.8	56.7	13.7
Air Force	300.3	60.0	29.9	47.7	43.9
U. S. Marine Corps	11.2	8.9	0.2	5.9	0.5
DLA	-	2.2	17.3	-	0.7
SOCOM	TBD	1.2	-	-	-
MDA	TBD	0.8	-	-	-

To facilitate preparation for existence and completeness audits, the Components have subdivided the mission critical asset categories into assessable units. Assessable units are classes, subcategories or groupings of assets that will be assessed for existence and completeness audit readiness. An assessable unit may also be organized around a system and its related processes, such as the Reliability and Maintainability Information System, which is used by the Air Force for aircraft. When an APSR defines the assessable unit, the scope of an audit includes all mission critical assets in that system.

Example assessable units for Military Equipment for the Air Force are:

- Aircraft
- Satellites and Satellite Launchers

- Intercontinental Ballistic Missiles
- Unmanned Aerospace Vehicles
- Externally-Carried Pods

Determining the assessable units is a key step in preparing for existence and completeness audits.

AUDIT READINESS DEFINED

Audit readiness will be achieved by conducting physical inventories utilizing acceptable sampling techniques, as described in the GAO Financial Audit Manual (FAM), and results in a minimum 95 percent accuracy rate. This accuracy rate is prescribed by the GAO FAM for auditors of Federal financial statements. For sensitive and classified assets, which include Military Equipment, the accuracy rate is 100 percent.

Audit readiness also includes validating the effectiveness of the Key Control Objectives (KCOs) applicable to the existence and completeness assertions. The role of KCOs in the audit readiness methodology is explained in Appendix 1.

In addition, the Components are validating the availability of acceptable supporting documentation for mission critical assets. When a Component asserts that an assessable unit is audit ready, it must submit assertion documentation to the OUSD(C) and DoD IG, who will review it and perform limited testing to validate that the assessable unit is ready for audit.

COMMON CHALLENGES

The Components must have strong controls associated with the processes and systems used to manage their mission critical assets. These controls must be tested and strengthened when determined to be ineffective or weak in order to sustain accuracy. Otherwise, progress could be undermined by invalid or unrecorded changes for additions and dispositions.

Other challenges the Components must address during Wave 3 include:

- Implementing standard units of measure,
- Accounting for reworked assets,
- Maintaining accountability over contractor-held assets,
- Identifying alternative procedures for validating E&C for deployed assets, and
- Implementing business rules for co-located facilities (joint basing).

AUDIT READINESS CAPABILITY BASELINE, STATUS AND PLANS

This section of the Report provides a summary-level view of the status and plans of the Army, Navy, Air Force and DLA to achieve Wave 3 audit readiness. The information is presented in three different figures per Component, as follows:

1. Audit Readiness Plans
2. Key Control Objective (KCO) Status and Projections
3. Key Supporting Documentation (KSD) Status and Projections

In addition to identifying the planned completion of audit readiness milestones (i.e., Audit Readiness Assertion, Validation, and Under Audit or Sustainment), the Audit Readiness Plans include the planned completion of the following Success Criteria/Key Capabilities:

1. Physical inventories meet audit standards,
2. Controls over recording asset acquisitions, disposals and transfers are effective,
3. Supporting documentation is retained and available to meet audit standards,
4. Financial and management data is reliable and accurate in system of record, and
5. Implement process, control and system improvements.

The status, as presented in the KCO and KSD figures, represents each Component's financial management capability baseline, that is, the effectiveness of their internal controls and ability to readily provide evidential matter to auditors as of the date of this Report. Over time, as the Components execute their FIPs, these tables and charts will reflect their progress from the baseline (as of March 31, 2010) to achieving audit readiness.

The KCO and KSD metrics track progress in achieving the end-state outcome of auditability. The KCO metrics reflect the Components' progress in achieving a strong internal control program that ensures financial transactions are timely and accurately recorded.

The KCO metrics provide management with visibility of the Components' assessment, testing and remediation activity until the KCOs have been determined to be effective. A standard set of KCOs are embedded in each of the Components' FIPs and have been linked to the discovery and corrective activities that identify them as either effective or a weakness.

KSD metrics capture the Components' progress in identifying supporting documentation deficiencies and problems that must be remediated before achieving auditability. Maintaining and making readily available acceptable evidential matter is critical to successful audits. This has been a long-standing deficiency in the Department, and resolving it is essential. The FIAR methodology provides guidance to assist in resolving this impediment and this metric tracks progress.

It is important to note that most of the reported status in the KCO and KSD figures that follow reflect zero percent (0%) assessed and zero percent effective. This means that, at the time of this Report, the Component FIPs did not reflect the outcome of such activity. The Components are in the process of updating their FIPs to reflect this activity, and the November 2010 FIAR Plan Status Report will present an updated status.

Each following Component section contains a summary table highlighting its strategy and other information pertaining to Wave 3, as well as information impacting the Component's approach, challenges or progress.

ARMY

Army	Highlights
Wave 3 Strategy	• Military Equipment: 4 asset types achieve existence and completeness audit readiness in second quarter of FY 2011; full audit readiness in first quarter FY 2015. • Ensuring compliance with established Office of the Secretary of Defense and Army real property policy and guidance is a key step for implementing effective controls. • Asserting Real Property full audit readiness (all 5 management assertions), not working existence and completeness separately. • Inventory and OM&S audit readiness are dependent on the deployment of three ERPs (General Fund Enterprise Business System, Logistics Modernization Program, and Global Command Support System-Army), and therefore, Army will not assert audit readiness on existence and completeness separately from valuation.
Figure IV-2 Audit Readiness Plans	• Military Equipment: 4 asset types achieve audit readiness in second quarter of FY 2011; full audit readiness in first quarter FY 2015. • Real Property: Audit ready in first quarter of FY 2013. • Inventory: Audit ready in third quarter of FY 2015. • OM&S: Audit ready in third quarter of FY 2015. • General Equipment: Fire and Rescue Equipment existence and completeness audit ready in second quarter FY 2011; full audit ready in fourth quarter of FY 2014.
Figure IV-3 Key Control Objective (KCO) Status and Projections	• No KCOs have been assessed.
Figure IV-4 Key Supporting Documentation (KSD) Status and Projections	• No KSDs have been assessed.

Figure IV-2 Audit Readiness Plans

Army General Fund	FY10		FY11				FY12				FY13				FY14				FY15				FY16				FY17			
Assessable Unit	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
Military Equipment																														
Apache AH-64D			5																											
900 Series Small Tug			5																											
All Source Analysis System-Light			5																											
Aircraft Utility UC-35C			5																											
All Military Equipment Assertion																														
General Equipment																														
Fire & Rescue			5																											
All General Equipment Assertion																														
Inventory																														
OM&S																														
Real Property																														

Legend
- Audit Readiness Assertion
- Validation
- Under Audit or Sustainment

Success Criteria / Key Capability

1 Physical inventories meet audit standards
2 Controls over recording asset acquisitions, disposals and transfers are effective
3 Supporting documentation is retained and available to meet audit standards
4 Financial and management data is reliable and accurate in system of record
5 Implement process, control, and system improvements

Figure IV-3 E&C Key Control Objective (KCO) Status and Projections

Army Assessable Unit	# KCOs	% Assessed	% Effective
Military Equipment	6	0%	0%
Real Property	6	0%	0%
OM&S	6	0%	0%
Inventory	6	0%	0%
General Equipment	6	0%	0%

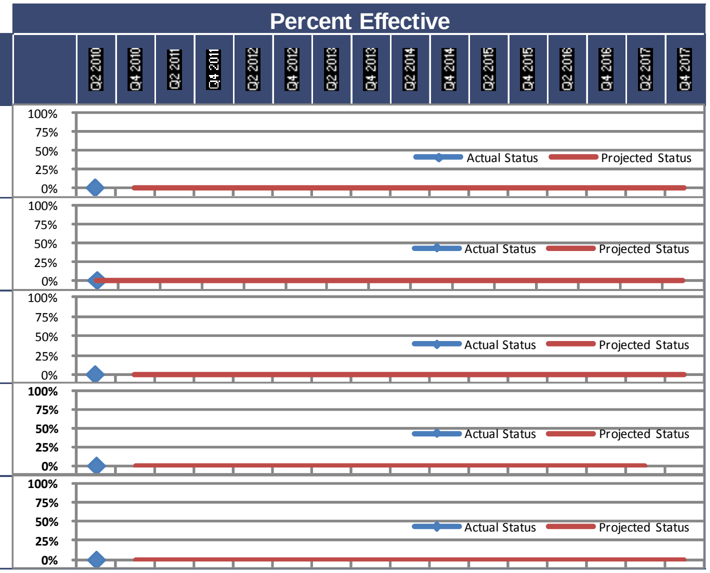
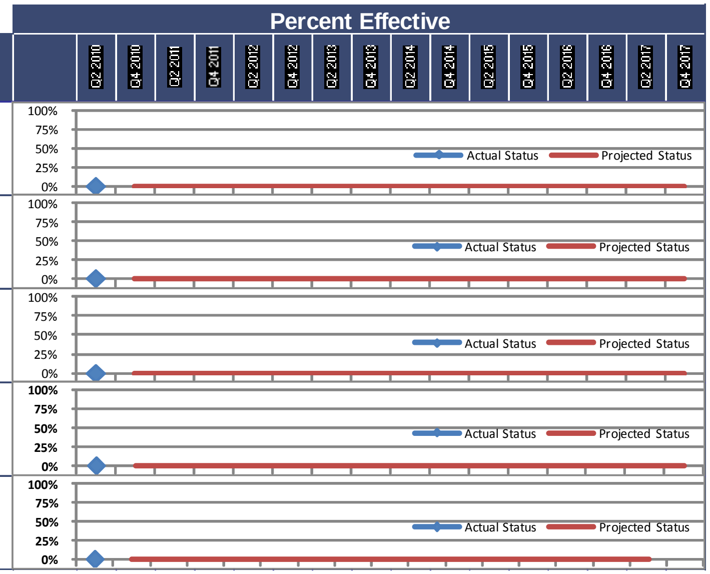


Figure IV-4. E&C Key Supporting Documentation (KSD) Status and Projections

Army Assessable Unit	# KSDs	% Assessed	% Effective
Military Equipment	4	0%	0%
Real Property	4	0%	0%
OM&S	4	0%	0%
Inventory	4	0%	0%
General Equipment	4	0%	0%



NAVY

Navy	Highlights
Wave 3 Strategy	• Aircraft, Ships, ICBMs and Satellites will be ready for audit by the end of FY 2010. • Existence and completeness will not be asserted separately for other asset categories. • Asserting Real Property full audit readiness (all 5 management assertions), i.e., not working existence and completeness separately. The completion of data cleansing and reconciliation is key to real property audit readiness. • Inventory and OM&S assertion dependent on the deployment of Navy ERP, and therefore, will not assert existence and completeness audit readiness separately from valuation. However, ammunition is maintained in a system not to be migrated into Navy ERP; therefore, Navy may assert on ammunition prior to achieving audit readiness for all OM&S.
Figure IV-5 Audit Readiness Plans	• Military Equipment: Audit ready in fourth quarter of FY 2010. • Real Property: Audit ready in second quarter of FY 2013. • Inventory: Audit ready in first quarter of FY 2013. • OM&S: Audit ready in second quarter of FY 2015. • General Equipment: Audit ready in fourth quarter of FY 2013.
Figure IV-6. Key Control Objective (KCO) Status and Projections	• Military Equipment: 100% of KCOs have been assessed. No KCOs are effective. • Real Property: 100% of KCOs have been assessed. No KCOs are effective. • Inventory: 100% of KCOs have been assessed. No KCOs are effective. • OM&S: 100% of KCOs have been assessed. No KCOs are effective. • General Equipment: No KCOs have been assessed.
Figure IV-7 Key Supporting Documentation (KSD) Status and Projections	• No KSDs have been assessed.

Figure IV-5 Audit Readiness Plans

Navy General Fund	FY10		FY11				FY12				FY13				FY14				FY15				FY16				FY17			
Assessable Unit	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
Military Equipment - Aircraft	5																													
Military Equipment - Ships	5																													
Military Equipment - ICBMS	5																													
Military Equipment - Satellites	5																													
Military Equipment - Final Assertion																														
General Equipment																														
OM&S																														
Inventory																														
Real Property																														

Legend
- Audit Readiness Assertion
- Validation
- Under Audit or

Success Criteria / Key Capability
1 Physical inventories meet audit standards
2 Controls over recording asset acquisitions, disposals and transfers are effective
3 Supporting documentation is retained and available to meet audit standards
4 Financial and management data is reliable and accurate in system of record
5 Implement process, control, and system improvements

Figure IV-6 E&C Key Control Objective (KCO) Status and Projections

Navy Assessable Unit	# KCOs	% Assessed	% Effective
Military Equipment	6	100%	0%
Real Property	6	100%	0%
OM&S	6	100%	0%
Inventory	6	100%	0%
General Equipment	6	0%	0%

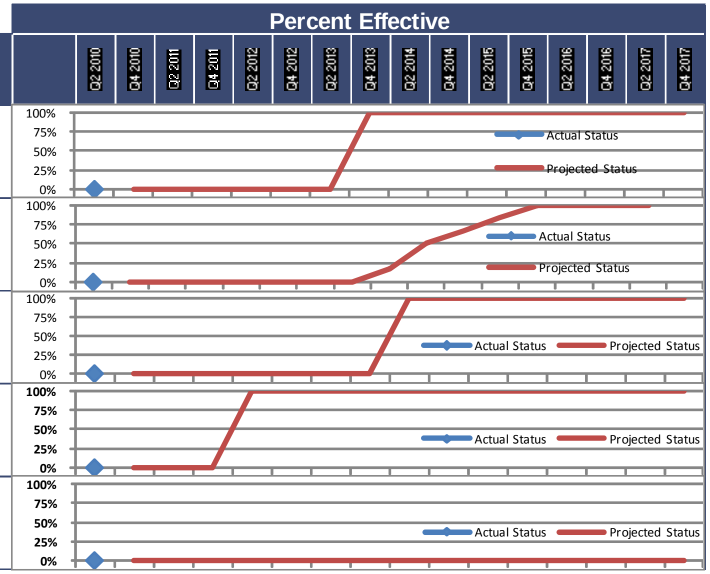


Figure IV-7 E&C Key Supporting Documentation (KSD) Status and Projections

Navy Assessable Unit	# KSDs	% Assessed	% Effective
Military Equipment	4	0%	0%
Real Property	4	0%	0%
OM&S	4	0%	0%
Inventory	4	0%	0%
General Equipment	4	0%	0%

AIR FORCE

Air Force	Highlights
Wave 3 Strategy	• Military Equipment (i.e., aircraft, satellites, ICBMs, UAVs and Pods) will be audit ready in Quarter 1 of FY 2011. • Asserting Real Property and Inventory full audit readiness (all 5 management assertions), i.e., not working existence and completeness separately. • Inventory and OM&S complete audit readiness depends on the deployment of the Expeditionary Combat Support System ERP.
Figure IV-8. Audit Readiness Plans	• Military Equipment: Audit readiness in first quarter of FY 2011. • Real Property: Audit ready in third quarter of FY 2013. • Inventory: Audit ready in fourth quarter of FY 2015. • OM&S: Audit ready for 3 asset categories in FY 2011. • General Equipment: Audit ready fourth quarter FY 2016.
Figure IV-9. Key Control Objective (KCO) Status and Projections	• Military Equipment: 100% of KCOs have been assessed and 100% determined to be effective. • Real Property, OM&S, Inventory and General Equipment: 100% of KCOs have been assessed. No KCOs are effective.
Figure IV-10 Key Supporting Documentation (KSD) Status and Projections	• Military Equipment: 100% of KSDs have been assessed and 100% have been determined to be effective. • Inventory: 100% of KSDs have been assessed and 100% have been determined to be effective.

Figure IV-8 Audit Readiness Plans

Air Force General Fund	FY10		FY11				FY12				FY13				FY14				FY15				FY16				FY17			
Assessable Unit	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4
Military Equipment		1,2,3,4,5																												
General Equipment																									1,2,3,4,5					
OM&S - Missile Motors		1,2,3,4,5																												
OM&S - Spare Engines			1,2,3,4,5																											
OM&S - Cruise Missiles & Drones				1,2,3,4,5																										
Inventory																					1,2,3,4,5									
Real Property												1,2,3,4,5																		

Legend
- Audit Readiness Assertion
- Validation
- Under Audit or Sustainment

Success Criteria / Key Capability
1 Physical inventories meet audit standards
2 Controls over recording asset acquisitions, disposals and transfers are effective
3 Supporting documentation is retained and available to meet audit standards
4 Financial and management data is reliable and accurate in system of record
5 Implement process, control, and system improvements

Figure IV-9 E&C Key Control Objective (KCO) Status and Projections

Air Force Assessable Unit	# KCOs	% Assessed	% Effective
Military Equipment	6	100%	100%
Real Property	6	100%	0%
OM&S	6	100%	0%
Inventory	6	100%	0%
General Equipment	6	100%	0%

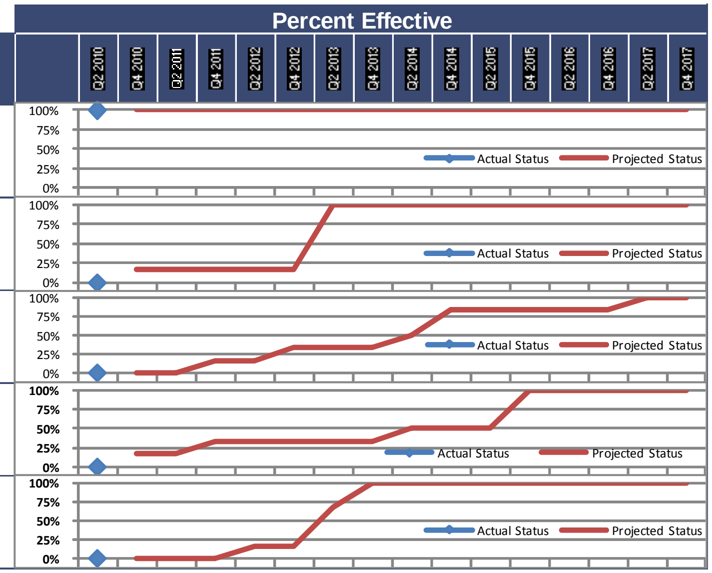
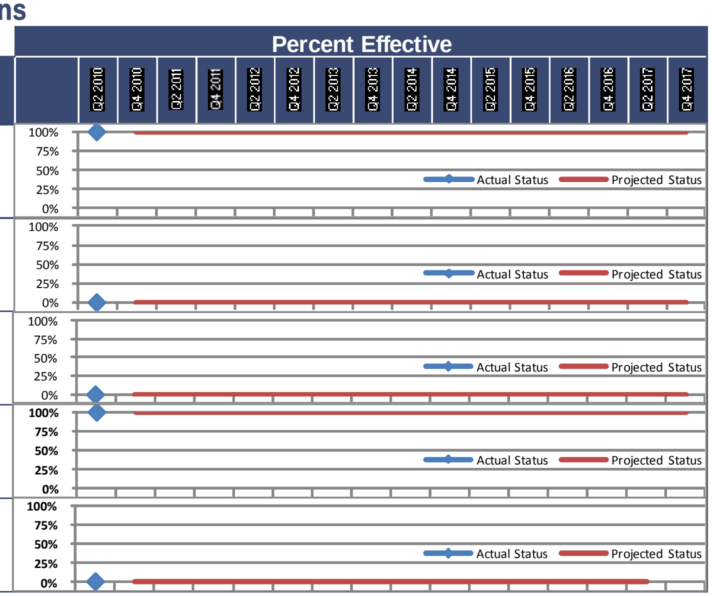


Figure IV-10 E&C Key Supporting Documentation (KSD) Status and Projections

Air Force Assessable Unit	# KSDs	% Assessed	% Effective
Military Equipment	4	100%	100%
Real Property	4	0%	0%
OM&S	4	0%	0%
Inventory	4	100%	100%
General Equipment	4	0%	0%



DLA

DLA	Highlights
Wave 3 Strategy	• Existence and completeness audit readiness will be asserted during FY 2014 as part of achieving complete auditability. • Real Property, Inventory and General Equipment audit ready assertions to be for all 5 management assertions, i.e., not working existence and completeness separately.
Figure IV-11. Audit Readiness Plans	• Real Property: Audit ready in second quarter of FY 2014. • Inventory: Audit ready in fourth quarter of FY 2014. • General Equipment: Audit ready in second quarter of FY 2014.
Figure IV-12 Key Control Objective (KCO) Status and Projections	• 100% of Real Property KCOs have been assessed. No KCOs are effective. • 83% of Inventory and General Equipment KCOs have been assessed. No KCOs are effective.
FigureIV-13. Key Supporting Documentation (KSD) Status and Projections	• No KSDs have been assessed.

Figure IV-11 Audit Readiness Plans

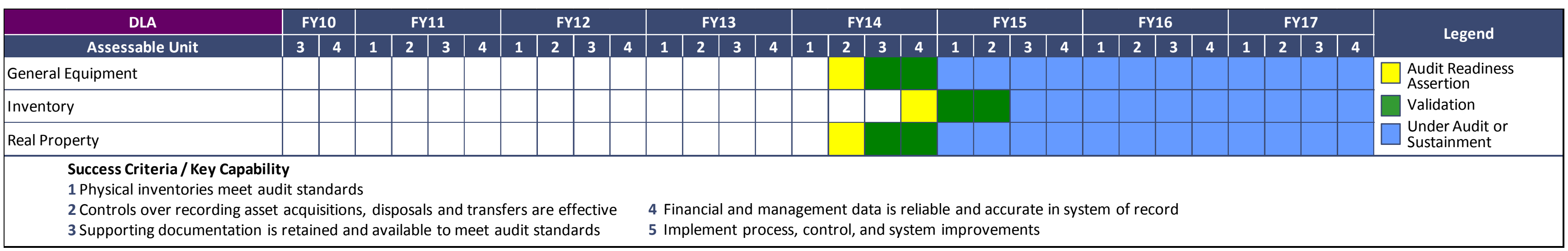


Figure IV-12. E&C Key Control Objective (KCO) Status and Projections

DLA Assessable Unit	# KCOs	% Assessed	% Effective
Real Property	6	100%	0%
Inventory	6	83%	0%
General Equipment	6	83%	0%

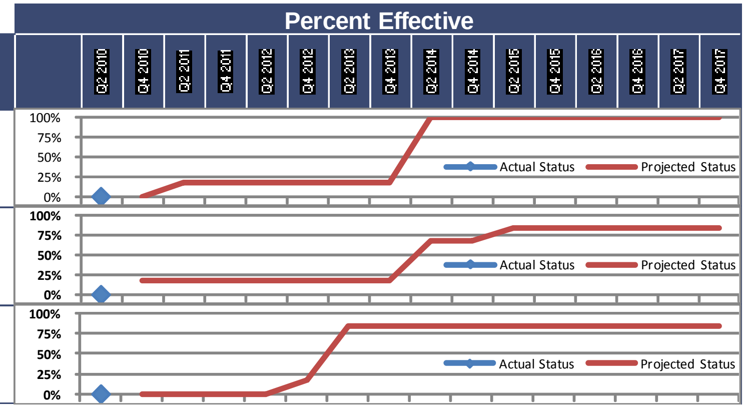
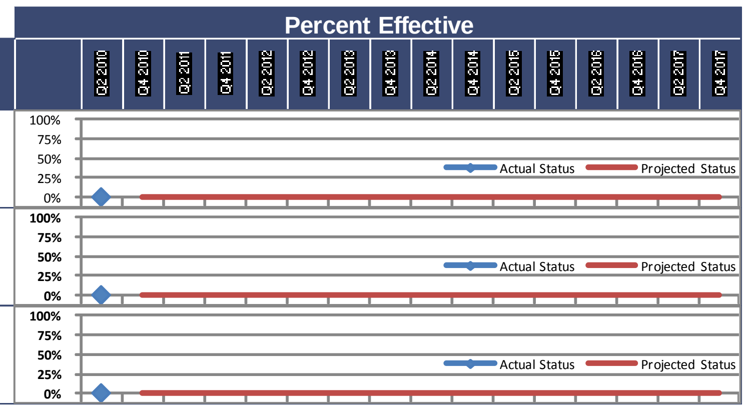


Figure IV-13 E&C Key Supporting Documentation (KSD) Status and Projections

DLA Assessable Unit	# KSDs	% Assessed	% Effective
Real Property	4	0%	0%
Inventory	4	0%	0%
General Equipment	4	0%	0%



PROGRESS METRICS

Results-oriented, progress metrics provide a useful means for management to monitor and measure financial improvement progress. This section of the Report provides two types of metrics:

- Metrics that measure progress by validations and audits, and
- Metrics that measure progress by improvements to mission critical asset management.

Progress Measured by Validations and Audits

Figure IV-14 provides the Department's current status and interim goals--those to be accomplished by the end of FY 2012--for achieving Wave 3 objectives. The figure also includes the assessable units for Wave 3.

Figure IV-14 shows that 43 percent of Wave 3 will be validated through independent examinations as audit ready by the end of FY 2012. The percentages are based on mission critical asset dollar values reported in the Department's FY 2008 financial statements.

Figure IV-14. FIAR Existence and Completeness Priority Status and Interim Goals

	FY 2009	FY 2010	FY 2011	FY 2012
Existence and Completeness Audit Ready	4%	4%	43%	43%
Assessable Units				
Military Equipment	0%	0%	37%	37%
Real Property	4%	4%	4%	4%
Inventory	0%	0%	0%	0%
Operating Material and Supplies	0%	0%	2%	2%
General Equipment	0%	0%	0%	0%

Progress Measured by Improvements to Mission Critical Asset Management

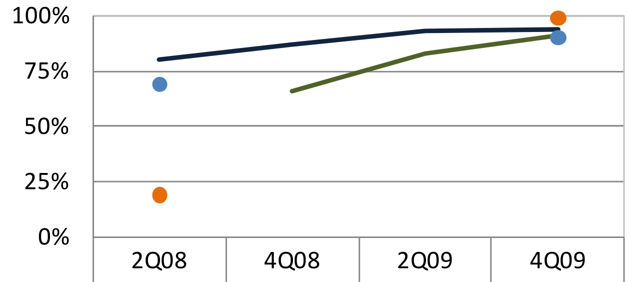
The second type of metric measures improvements to functions and capabilities that impact the management of mission critical assets. They either measure outcomes of better asset information (e.g., OM&S Release Denial Rate) or measure progress improvements needed to achieve better asset information (e.g., Equipment Contracts Compliant with IUID).

Each of the metrics that follows includes a description, goal, benefits, and results. These metrics include the following:

- Figure IV-15 Equipment Contracts Compliant with IUID
- Figure IV-16 Proper Financial Accounting Treatment for Military Equipment Compliance
- Figure IV-17 Serial Management and Accounting of Group and Composite Programs
- Figure IV-18 Real Property Asset Reconciliation
- Figure IV-19 Real Property Physical Inventory Completion
- Figure IV-20 Physical Inventory Adjustments – Real Property
- Figure IV-21 Inventory Valued at Moving Average Cost
- Figure IV-22 Physical Inventory Adjustments – Inventory
- Figure IV-23 OM&S Valued at Moving Average Cost
- Figure IV-24 OM&S Release Denial Rate
- Figure IV-25 OM&S Found on Post
- Figure IV-26 Physical Inventory Adjustments – OM&S

Figure IV-15.

Equipment Contracts Compliant with IUID



	2Q08	4Q08	2Q09	4Q09
Army		66%	83%	91%
Navy	80%	87%	93%	94%
Air Force	69%			90%
USSOCOM	19%			99%

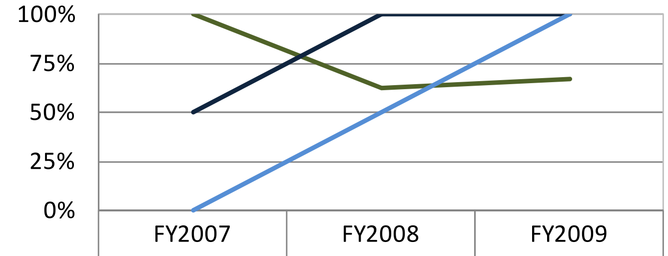
Metric Title: Equipment Contracts Compliant with IUID
Wave 3 - Existence and Completeness

Description:
DoD policy requires that contracts for DoD assets include a requirement for contractors to mark assets with a unique item identifier (UII) upon delivery to the government. A directive was given in December 2007 for Components to report contract compliance in a Score Card to the Defense Procurement and Acquisition Policy (DPAP) Office. This metric tracks the percentage of contracts compliant by Component as reported to DPAP.
Goal:
100% IUID contract compliance.

Benefit:
Compliance with this requirement supports audit readiness and the tracking of DoD assets. Improving DoD asset visibility and traceability provides more accurate data to support management decisions for improved readiness for military missions.
Results:
Data has not been collected for all periods but the overall trend indicates increased compliance.

Figure IV-16.

Proper Financial Accounting Treatment for Military Equipment Compliance

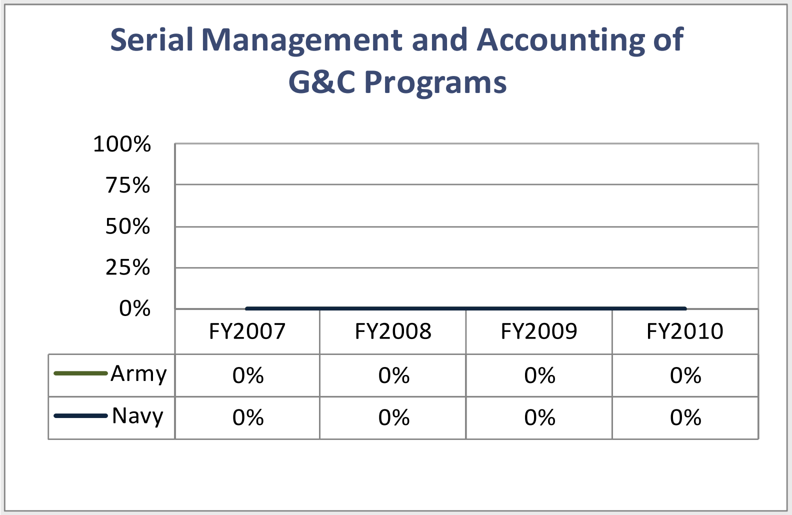


	FY2007	FY2008	FY2009
Army	100%	63%	67%
Navy	50%	100%	100%
Air Force	0%	50%	100%

Metric Title: Proper Financial Accounting Treatment for Military Equipment Compliance
Wave 3 - Existence and Completeness / Wave 4 - Valuation

Description:
DoD policy requires that Military Equipment (ME) contracts be structured to permit the proper accounting treatments to be applied for determining an accurate full cost as required by SFFAS No. 6 and DoDI 5000.64.
Goal:
100% of new ME procurement contracts be in compliance with the policy beginning in FY 2007.
Benefit:
Compliance with this requirement supports audit readiness and improves information available to decision makers by providing more accurate information to support procurement decisions.
Results:
Sample sizes are small which can result in variations from year to year. However, the overall trend shows increased compliance.

Figure IV-17.



	FY2007	FY2008	FY2009	FY2010
Army	0%	0%	0%	0%
Navy	0%	0%	0%	0%

Metric Title: Serial Management and Accounting of Assets of Group and Composite Programs

Wave 3 - Existence and Completeness

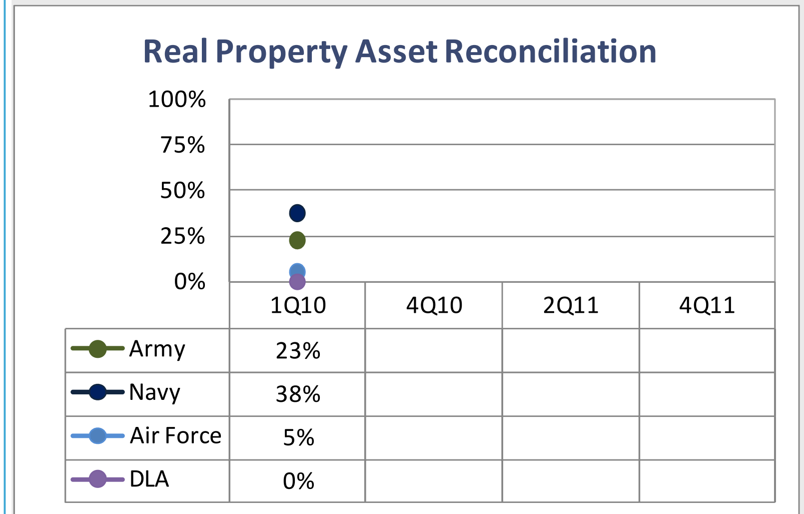
Description:
DoDI 5000.64 requires property to be managed at the serial or individual asset level. Currently, military equipment programs that are not serially managed are valued and accounted for in asset accounting systems at the program/Group and Composite (G&C) level, resulting in the loss of the ability to track individual asset values and statuses. The Air Force does not currently have any G&C programs and is therefore excluded from this metric.

Goal:
Eliminate G&C program level tracking in asset accounting systems by inventorying assets within G&C programs and recording them at the asset /serial number level.

Benefit:
Tracking assets at the serial level increases the accuracy of property records and financial statements.

Results:
No data was received for this metric. Components will continue to obtain data for future status reports.

Figure IV-18.



	1Q10	4Q10	2Q11	4Q11
Army	23%			
Navy	38%			
Air Force	5%			
DLA	0%			

Metric Title: Real Property Asset Reconciliation

Wave 3 - Existence and Completeness

Description:
In accordance with DoDI 4165.14, all DoD real property data must be reconciled between the Defense Agencies and Military Services. This metric displays the percent of Components' real property information compliant with this requirement.

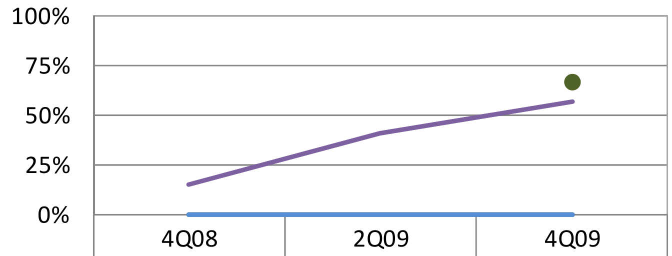
Goal:
100% of Defense Agencies' real property assets reconciled by the end of FY11.

Benefit:
Having real property reconciled will provide management with better access to accurate and complete data which will facilitate better decision making and support audit readiness.

Results:
Initial results show that data reconciled is currently below 50%. Trends will become apparent in future status reports.

Figure IV-19.

Real Property Physical Inventory Completion



	4Q08	2Q09	4Q09
Army			67%
Navy	0%	0%	0%
Air Force	0%	0%	0%
DLA	16%	41%	57%

Metric Title: Real Property Physical Inventory Completion
Wave 3 - Existence and Completeness

Description:
DoDI 4165.14 requires Components to inventory all real property assets at least every five years. This metric shows the percentage of Components' real property inventoried within a 5 year time span against the total number of reported assets.

Goal:
Physical inventory of 100% of real property assets over a five year period.

Benefit:
Ensuring that all real property is inventoried is important for audit readiness. It is especially pertinent to completeness but assists other assertions as well. This metric provides a status on how several material Components are complying with this important control activity.

Results:
Data was not available for Navy and Air Force. The Army percentage is an overall estimate for the past two years. DLA is trending upward.

Figure IV-20.

Physical Inventory Adjustments - Real Property

	FY2009	FY2010	FY2011	FY2012
Army	0.3%			
Navy	0.7%			
Air Force	0.1%			

Metric Title: Physical Inventory Adjustments - Real Property
Wave 3 - Existence and Completeness

Description:
DoDI 4165.14 requires Components to inventory all real property assets at least every five years. This metric shows the percentage of a Component's real property asset records that are either added (found on post, inventory adjustment) or archived (loss by inventory) from its real property inventory. Significant additions or deletions as a result of inventory activities can be an indicator of internal control weaknesses.

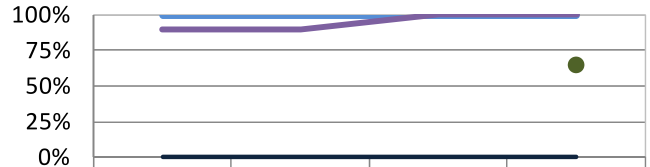
Goal:
Physical inventory process confirms the effectiveness of the acquisition and disposal processes and results in no adjustments.

Benefit:
Accurate property records enable managers to effectively plan for and execute the DoD mission.

Results:
Initial results show that adjustments to Real Property resulting from inventory are less than 1% of asset quantity.

Figure IV-21.

Inventory Valued at Moving Average Cost



	2Q08	4Q08	2Q09	4Q09
Army				65%
Navy	0%	0%	0%	0%
Air Force	100%	100%	100%	100%
DLA	90%	90%	100%	100%

Metric Title: Inventory Valued at Moving Average Cost

Wave 4 - Valuation

Description:
This metric shows the Components' status as a percentage of dollars for valuing appropriate inventory at a moving average cost. This costing method is used in conjunction with a perpetual inventory system. A weighted average cost per unit is recalculated following each purchase. This costing method is required by DoD.

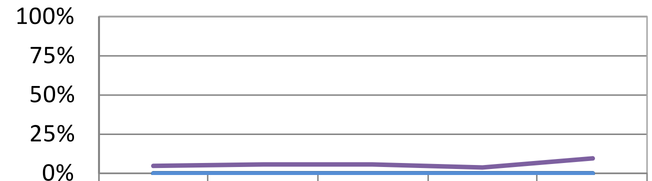
Goal:
100% of Inventory valued at a moving average cost where applicable.

Benefit:
Valuing inventory at moving average cost will bring DoD into compliance with current Federal accounting standards and DoD regulations. It will also provide users of financial reports the most accurate picture of the actual value of inventory in stock.

Results:
Air Force and DLA data indicate full compliance. Navy is currently at 0%. Army provided an estimate with several qualifications.

Figure IV-22.

Physical Inventory Adjustments - Inventory



	2Q08	4Q08	2Q09	4Q09	2Q10
Army	0%	0%	0%	0%	0%
Navy	0%	0%	0%	0%	0%
Air Force	0%	0%	0%	0%	0%
DLA	4%	6%	6%	4%	10%

Metric Title: Physical Inventory Adjustments - Inventory

Wave 3 - Existence and Completeness

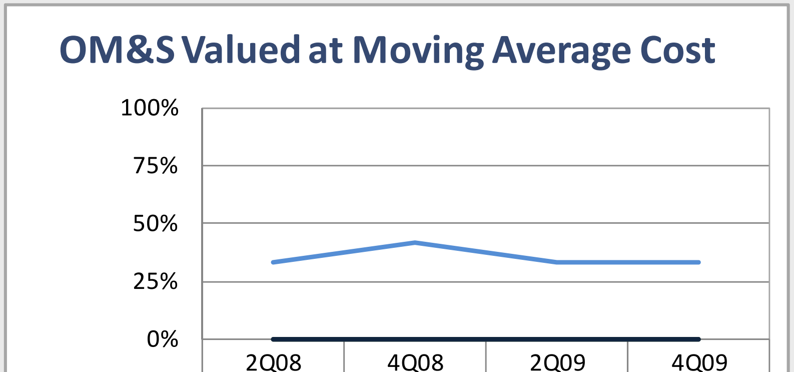
Description:
Inventory is periodically counted to ensure stock levels are accurate. This metric shows the percentage of a Component's inventory balance that is adjusted as a result of physical inventory activities during a six month time period. Significant adjustments as a result of inventory activities can be an indicator of internal control weaknesses. Poor acquisition controls can result in positive adjustments, while poor controls over inventory disposal can result in negative adjustments.

Goal:
Have sufficient controls in place so that physical inventories confirm the accuracy of inventory records and result no material adjustments.

Benefit:
Accurate inventory records enable commanders and managers to effectively plan for and execute the DoD mission.

Results:
DLA adjustments range from 4-10% of inventory quantity. Other Components were not able to provide data, but will continue to acquire it for future status reports.

Figure IV-23.



	2Q08	4Q08	2Q09	4Q09
Army	0%	0%	0%	0%
Navy	0%	0%	0%	0%
Air Force	33%	42%	33%	33%

Metric Title: OM&S Valued at Moving Average Cost
Wave 4 - Valuation

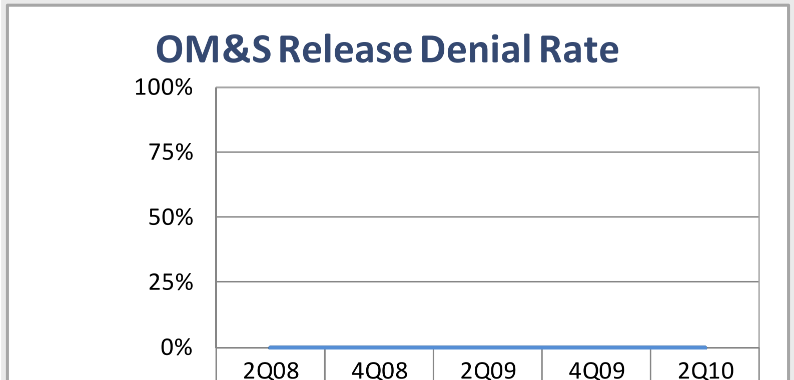
Description:
This metric shows the Components' status as a percentage of dollars for valuing appropriate operating material and supplies at a moving average cost. This costing method is used in conjunction with a perpetual inventory system. A weighted average cost per unit is recalculated following each purchase. This costing method is required by DoD.

Goal:
100% of OM&S valued at a moving average cost.

Benefit:
Valuing OM&S at moving average cost will bring DoD into compliance with current Federal accounting standards and DoD regulations. It will also provide users of financial reports the most accurate picture of the actual value of OM&S in stock.

Results:
Air Force results are level. Navy reports 0%. No data was obtained from Army.

Figure IV-24



	2Q08	4Q08	2Q09	4Q09	2Q10
Army	0%	0%	0%	0%	0%
Navy	0%	0%	0%	0%	0%
Air Force	0%	0%	0%	0%	0%

Metric Title: OM&S Release Denial Rate
Wave 3 - Existence and Completeness

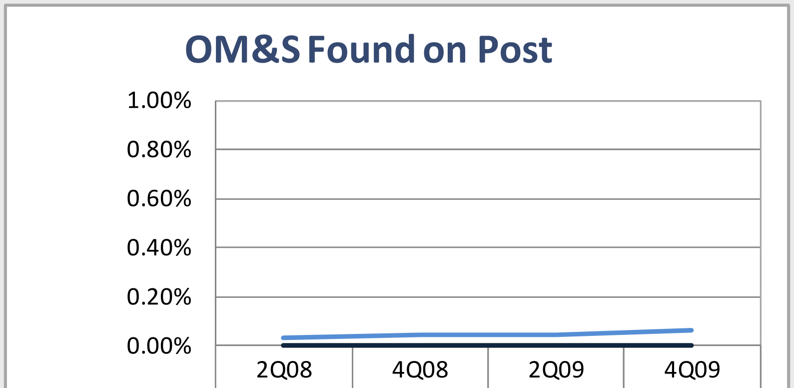
Description:
This metric displays the percentage of requested OM&S orders that were not shipped by a warehouse or distribution center due to the requested assets not being of the type, quantity or location indicated in the system. While there are appropriate reasons to deny the release of OM&S, denials as a result of inaccurate records are an indication of poor controls related to asset existence.

Goal:
Denial rates due to inaccurate records reach 0%.

Benefit:
Tracking denial rates provides visibility into a critical function of OM&S management. OM&S records and quantities need to be accurate to ensure that supplies are refreshed and available when needed for missions.

Results:
No data provided. Components are continuing to obtain data for this metric.

Figure IV-25.



	2Q08	4Q08	2Q09	4Q09
Army	0.00%	0.00%	0.00%	0.00%
Navy	0.00%	0.00%	0.00%	0.00%
Air Force	0.03%	0.05%	0.05%	0.06%

Metric Title: OM&S Found on Post
Wave 3 - Existence and Completeness

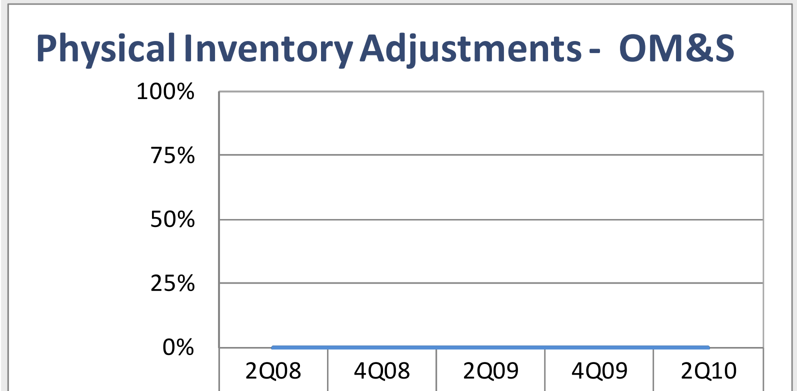
Description:
Operating materials and supplies are periodically counted to ensure stock levels are kept accurate. When significant amounts of previously unrecorded assets are found, it can be an indication of poor controls around acquisition and an inability to sustain completeness. This metric displays the quantities of OM&S that have been found on post over the period.

Goal:
Minimize the amount of OM&S found on post to immaterial values that do not impact missions.

Benefit:
This metric provides insight into the effectiveness of controls during the acquisition of OM&S. When effective controls are in place, OM&S is more likely recorded accurately and is less likely to be found on post.

Results:
Air Force OM&S found on post is consistently less than 1%. Other Components did not obtain data in time for this status report.

Figure IV-26.



	2Q08	4Q08	2Q09	4Q09	2Q10
Army	0%	0%	0%	0%	0%
Navy	0%	0%	0%	0%	0%
Air Force	0%	0%	0%	0%	0%

Metric Title: Physical Inventory Adjustments - OM&S
Wave 3 - Existence and Completeness

Description:
Operating material and supplies are periodically counted to ensure stock levels are accurate. This metric shows the percentage of a Component's OM&S balance that is adjusted as a result of physical inventory activities during a six month time period. Significant adjustments as a result of inventory activities can be an indicator of internal control weaknesses. Poor acquisition controls can result in positive adjustments, while poor controls over OM&S usage can result in negative adjustments.

Goal:
Have sufficient controls in place so that physical inventories confirm the accuracy of OM&S records and result in no material adjustments.

Benefit:
Accurate OM&S records enable commanders and managers to effectively plan for and execute the DoD mission.

Results:
No data received. Components will continue to acquire data for future status reports.

Appendix 1. FIAR Audit Readiness Strategy and Methodology

A clear, comprehensive strategy for achieving audit readiness is critical to ensuring limited resources are assigned effectively to facilitate measurable and sustainable progress. The FIAR Audit Readiness Strategy provides a critical path for the Department while balancing the need to achieve short-term accomplishments with the long-term goal of an unqualified opinion on the Department's financial statements.

The FIAR Audit Readiness Strategy is consistent with, and focuses improvement work on, the objectives and priorities established by the USD(C), which require the Department to first focus on improving financial and business information most useful to DoD management and warfighters. The USD(C) priorities are to improve budgetary information and mission critical asset information. Both of these priorities are specifically addressed and prioritized within the FIAR Audit Readiness Strategy.

Each of the Department's material financial statement line items have unique and complex accounting and auditing challenges and issues that must be overcome before auditability can ultimately be achieved. The FIAR Audit Readiness Strategy groups and prioritizes the material business processes (that result in activity reported on various financial statement line items) within one of five waves, and then summarizes steps each Component should take to address each wave. The waves and steps are prioritized based on USD(C) priorities, known issues and the dependencies of financial statements, line items and business processes on one another.

The Department's Audit Readiness Strategy draws from the strengths of several alternative approaches and groups individual end-to-end processes into one or multiple waves. Efforts are prioritized within each wave by end-to-end processes including corresponding line-items reported on other financial statements, as well as by dependencies. This strategy provides coverage of all financial statements, while prioritizing and improving first the information most often used by DoD management. Furthermore, the five distinct waves lead to interim audit readiness milestones, and ultimately, to a full-scope financial statement audit. The Components are ensuring appropriate controls are in place and operating effectively for relevant financial reporting processes prior to asserting each wave as complete (e.g., controls over the presentation and disclosure over the SBR must be asserted ready at the end of Wave 2).

The five distinct waves that comprise the FIAR Audit Readiness Strategy lead to audit readiness milestones that will be validated by an independent auditor once controls are in place and operating effectively, and the appropriate management assertions have been made.

THE AUDIT READINESS STRATEGY "WAVES"

The Audit Readiness Strategy "waves" representing significant levels of effort and accomplishments are:

- Wave 1 - Appropriations Received Audit
- Wave 2 - Statement of Budgetary Resources (SBR) Audit
- Wave 3 - Mission Critical Asset Existence and Completeness Audit
- Wave 4 - Full Financial Statement Audit, Except for Legacy Assets (New Asset Valuation)
- Wave 5 - Full Financial Statement Audit

Waves 1, 2 and 3 are being worked concurrently, as shown in Figure A1-1.

Figure A1-1 Audit Readiness and Priority Strategy

Wave 1 - Appropriations Received Examination

Wave 1 focuses on the processes and controls associated with the appropriation of funds from the Congress to the Department. Completing Wave 2 depends on the successful completion of Wave 1.

Wave 1 is critically important to the Department's overall financial improvement efforts, because it is the first step in receiving, recording and tracking the funds provided to the Department to accomplish its mission. Recognizing the importance of this critical first step, the Under Secretary of Defense (Comptroller) specifically directed that the Components focus initially on Wave 1 and work to prepare it for examination by the DoD Inspector General or an Independent Public Accountant by the end of FY 2010.

Financial management benefits of completing Wave 1 are:

1. Improves the accuracy and reliability of appropriated funds recorded in DoD systems, and
2. Assures accuracy in the prior year funding amounts reported in the Department's annual President's Budget.

Wave 2 - Statement of Budgetary Resources Audit

Wave 2 includes several end-to-end processes that are separated into assessable units each of which must be audit ready before the SBR can be audited. For example, cash disbursements within the Procure-to-Pay process and cash receipts within the Order-to-Cash process must be remediated before the Fund Balance with Treasury (FBWT) Balance Sheet line item can be audit ready. Also, the Procure-to-Pay process must be effective to ensure that Accounts Receivable recorded as a result of reimbursable activity (in the Order-to-Cash process) is accurate. Ultimately, successful remediation of the Assessable Units leads to an audit ready SBR.

Financial management benefits of completing Wave 2 are:

1. Improves the visibility of budgetary transactions ensuring a more effective use of limited resources,
2. Provides operational efficiencies through more readily available and accurate cost and financial information (e.g., more accurate obligation data for the Planning, Programming, Budgeting, and Execution process and fewer unmatched disbursements),
3. Improves fiscal stewardship through reduced improper payments,
4. Improves budget processes and controls thus reducing Antideficiency Act violations, and
5. Links execution to the President's Budget thus providing more consistency with the financial environment.

Wave 3 - Mission Critical Asset Existence and Completeness Audits

The audit readiness focus of this wave is primarily on the existence and completeness assertions, but also includes Rights and Obligations and portions of the Presentation and Disclosure assertions. Interdependencies between remediation of the receipt of goods and services processes included in the Procure-to-Pay process in Wave 1 helps ensure the sustainability of the existence and completeness assertions in future periods, especially for assessable units with a high volume of purchasing activity.

The benefits of completing Wave 3 are:

1. Moves the Department closer to achieving its long-standing goal of total asset visibility,
2. Improves the reliability and accuracy of the logistics supply chain and inventory systems, which ensures items needed by the warfighter are on-hand when needed and not procured unnecessarily,
3. Improves the ability to timely acquire, maintain and retire assets,
4. Provides better management information about assets, and
5. Ensures better control over assets, preventing their misuse, theft or loss.
6. Reduces unnecessary reordering.

Wave 4 - Full Audit Financial Statements, Except for Legacy Assets (New Asset Valuation)

Wave 4 includes the valuation assertion over new asset acquisitions and depends on the successful completion of Wave 3, requiring the existence and completeness assertions to be remediated before the valuation assertion can be completed. Also, proper contract structure for cost accumulation and cost accounting data must be in place prior to completion of the valuation assertion for new acquisitions.

The financial management benefits of completing Wave 4 are:

1. Moves the Department closer to achieving its long-standing goal of obtaining an unqualified opinion on all of its financial statements,
2. Provides more reliable and accurate logistics supply chain information on the cost of Inventory items and Operating Materials and Supplies (OM&S),
3. Improves the quality of information used by management when making operational decisions about capital investments in Military Equipment and General Equipment.

Wave 5 - Full Financial Statement Audit

Wave 5 focuses on the valuation of legacy assets. Once the Components have asserted effective controls over valuation of new acquisitions of Military Equipment, Real Property, Inventory, OM&S, and General Equipment, they will focus on valuing legacy assets. This sequencing of efforts ensures that controls are in place to go forward before addressing legacy assets. Legacy asset valuation depends on the availability of adequate supporting documentation to support appropriate cost accumulation by asset. Successful remediation of assertions related to existence and compltenness and valuation will allow the Components to support a full-scope financial statement audits.

METHODOLOGY

The Department's methodology for achieving improved financial information and auditability has evolved and been refined since the FIAR Plan was first issued in 2005. The methodology is now more focused, effective and consistent across the Components. Regardless of this evolution, much of the methodology remains the same, such as:

- Guided by Business Rules,
- Integrated with the implementation of OMB Circular A-123, Appendix A,
- Integrated with the modernization of business and financial systems, and
- Comprehensive by focusing improvements on policies, processes, controls, systems, data, audit evidence, and human capital.

The Business Rules, which drive a mandatory, standard step-by-step approach to achieving audit readiness, have been updated to incorporate lessons learned from earlier audit readiness initiatives, and two other important changes to the methodology have been made, as follows:

- Identification of, and focus on, Key Control Objectives (KCOs) and Key Supporting Documentation (KSD) as a primary outcome of financial improvement activities, and
- Use of a standard framework for Component Financial Improvement Plans (FIPs) that incorporates the modified Business Rules.

The modifications to the Business Rules, which are now referred to as the Audit Readiness Phases, and the two above changes are discussed below.

FIAR Audit Readiness Methodology Phases and Key Tasks

Before publication of the FIAR Plan in 2005, the Department developed "Business Rules" that required the Components to execute a phased approach to achieving auditability. The Business Rules also established a process for the OUSD(C) and Department of Defense Inspector General (DoD IG) to evaluate the audit readiness of a Component before a financial statement audit was initiated. This process lessened the risk that the audit would not be successful.

The Business Rules have been refined and are presently referred to as phases within the FIAR Audit Readiness Methodology. The methodology provides a step-by-step, approach to achieving improved financial information and audit readiness. Figure A1-2 provides a graphical depiction of the phases and the key tasks within each phase.

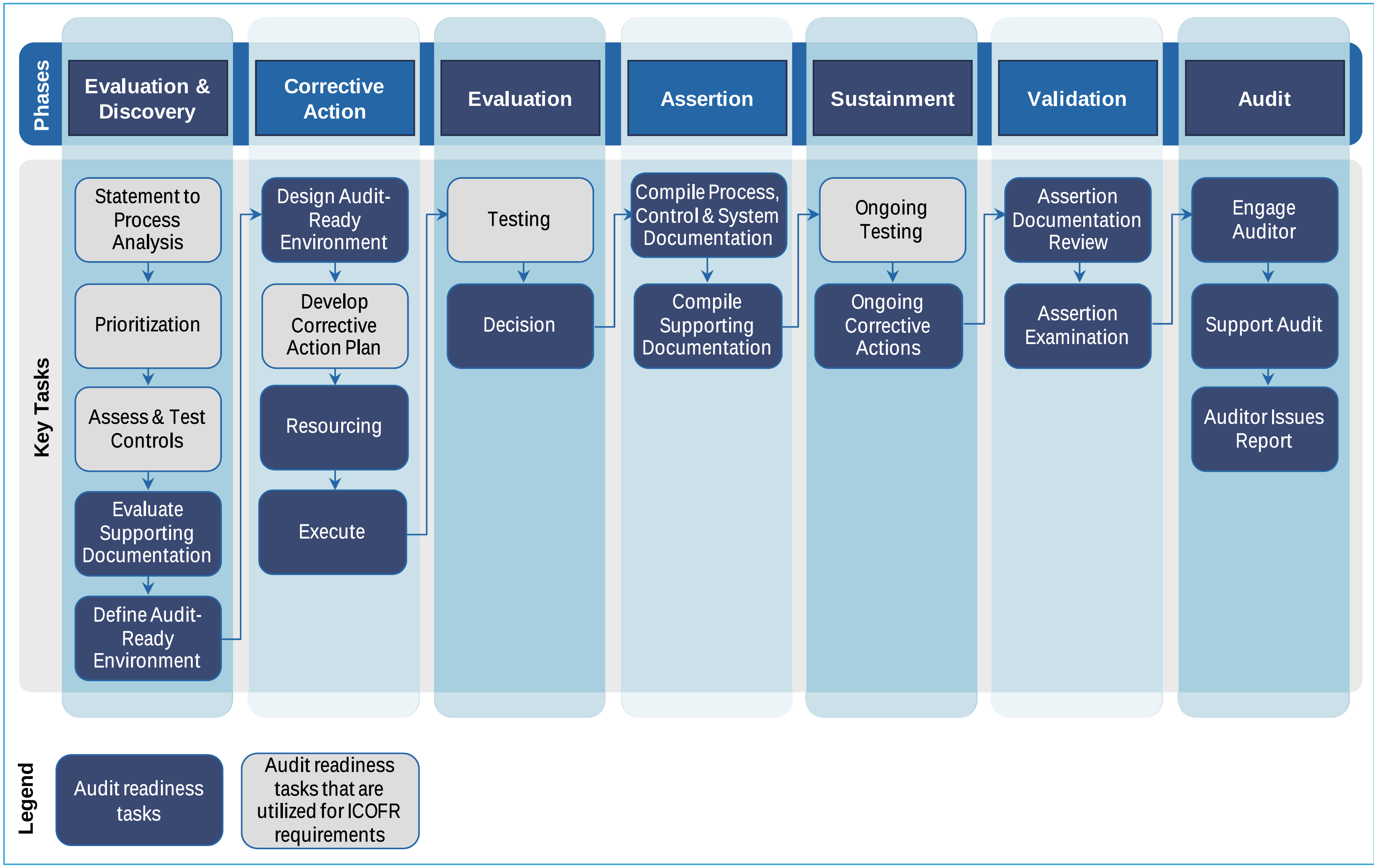
The phases and key tasks can be applied uniformly regardless of the size, materiality or scope of an assessable unit, and are as follows:

1. Evaluation and Discovery: Management maps its business and financial environment, assesses risks and tests controls, evaluates supporting documentation, identifies weaknesses and deficiencies, and defines its audit readiness environment.
2. Corrective Action: Management develops and executes corrective action plans/FIPs that include implementation of the audit ready environment, solutions to resolve deficiencies and weaknesses, and tests and strengthens internal controls.
3. Evaluation: Management evaluates corrective action effectiveness through testing and decides if it is ready to assert audit readiness.
4. Assertion: Management asserts audit readiness to the OUSD(C)/FIAR and DoD IG who evaluate the assertion and decide whether to proceed with an audit.
5. Sustainment: Management maintains audit readiness through risk based periodic testing of internal controls utilizing the OMB Circular A-123, Appendix A, process and procedures, and resolves any identified weaknesses.
6. Validation: OUSD(C)/FIAR, DoD IG or Independent Public Accountant (IPA) tests and validates audit readiness.
7. Audit: DoD IG or IPA audits the assessable unit or financial statements.

This step-by-step phased methodology delineates responsibilities between management and the auditors. Management's responsibilities focus on completing discovery and correction, asserting audit readiness of assessable units or financial statements, sustaining improvements, and asserting audit readiness (phases 1, 2, 3, 4 and 5). The OUSD(C)/FIAR, DoD IG or independent auditors validate audit readiness (phase 6), and the DoD IG or an IPA performs the audit of the assessable unit or financial statements (phase 7).

Detailed information explaining the FIAR Methodology to include the phases and key tasks can be found in the FIAR Guidance document issued by the OUSD(C). The FIAR Guidance document can be found on the Department's FIAR website of: http://comptroller.defense.gov/FIAR/index.html.

Figure AI-2. FIAR Methodology Phases and Key Tasks



Appendix 2. NDAA for Fiscal Year 2010 Required Information

The National Defense Authorization Act (NDAA) for FY 2010 directs the Department to prepare a report semi-annually on the status of the implementation of the FIAR Plan and to deliver it to the congressional defense committees not later than May 15 and November 15. The NDAA for FY 2010 also requires the Department to provide a report on the *actions taken* or *planned actions* and to address specific issues. In this section, the Department reports on its efforts to:

- Develop standardized guidance for Component Financial Improvement Plans (FIPs).
- Establish a baseline of financial management capabilities and weaknesses at the Component level.
- Provide results-oriented metrics for measuring and reporting quantifiable results toward addressing financial management deficiencies.
- Define the oversight roles of the Chief Management Officer (CMO) of the Department and CMOs of the Military Departments and other elements of the Department to ensure the requirements of the FIAR Plan are carried out.
- Assign accountability for carrying out specific elements of the FIAR Plan to the appropriate officials and organizations at the Component level.
- Develop mechanisms to track budgets and expenditures for the implementation of the requirements of the FIAR Plan.
- Develop a mechanism to conduct audits of the military intelligence programs and agencies and to submit their financial statements to the Congress.

The actions taken and planned actions for each of the above requirements follow.

STANDARD FIAR GUIDANCE

Actions Taken

Working collaboratively with the Components, the FIAR Directorate, OUSD(C), developed and issued to the Components the following:

- Detailed, standard guidance prescribing a mandatory methodology to be used by the Components to achieve the FIAR goals, objectives and priorities, and
- A standard framework and template for Component FIPs.

In addition to issuing standard guidance, the FIAR Directorate, OUSD(C), also took the following related actions:

- Developed a FIP for an SBR assessable unit for the Army and is now assisting the Army execute the plan,
- Assisted the OUSD(AT&L) develop and begin to execute an existence and completeness test plan for Air Force aircraft,
- Performed an analysis to identify material DoD-wide entities,
- Worked with the OUSD(AT&L) and Components to identify progress metrics, and
- Kicked off a DoD-wide FIAR change management and communications strategy and plan.

Details of these actions are discussed below.

Standard FIAR Guidance

To provide clearer guidance to the Components, shared Service Providers and executive agents, all of whom are working towards the goal of audit readiness, the FIAR Directorate, working collaboratively with the Components and utilizing the FIAR Subcommittee, prepared a comprehensive guidance document. The first draft was issued for coordination on December 23, 2009, and the final version is planned to be issued by May 14, 2010.

The guidance defines the Department's FIAR goals, strategy and methodology for becoming audit ready. The guidance also details the roles and responsibilities of all key participants and stakeholders. It includes a standard FIP framework and template, explained below, with measureable outcomes (KCOs) and requires the inclusion of systematic, standard FIAR phases and key tasks. The KCOs are discussed in detail in the guidance and provide the Components with instructions on how to revise their FIPs to conform to the standard framework and template.

The FIAR Guidance document was developed with the end users in mind and also serves as a handbook and training tool for existing and new users involved in audit readiness initiatives.

A copy of this document can be found at on the FIAR website at: http://comptroller.defense.gov/FIAR/index.html.

Standard FIP Framework and Template

The standard FIP framework and template require the Components to structure their FIPs in accordance with a detailed, systematic and phased methodology. Some of the key requirements of the framework and template that the Components must include in their FIPs are:

- Measureable outcomes (KCOs) linked to the FIP tasks for achieving the outcomes,
- Status (e.g., effective, weakness) of the KCOs,
- Baseline start and finish dates to track original task completion dates as the FIPs are revised or updated,
- Accountable people and organizations for FIP tasks, and
- Resource requirements to accomplish FIP tasks.

The Components have revised their FIPs for their priority assessable units and are in varying stages of revising their FIPs for other assessable units to conform to the standard framework.

The Components' standardized FIPs are maintained in the web-based FIAR Planning Tool (FIAR-PT), which provides the FIAR Directorate immediate access to the FIPs. This capability provides the FIAR Directorate the ability to review the FIPs and provide feedback and assistance, to share approaches and lessons learned between the Components, and to monitor the FIPs and report progress. The GAO also has access to the FIAR-PT.

Planned Actions

Because of its complexity, the guidance will need to be regularly updated and reissued.

In addition, the guidance was developed to be used not only as a reference document, but also as a handbook and training document. Accordingly, training needs to be developed, scheduled and conducted.

Planned actions are to:

- Update the guidance and re-issue it as needed, and
- Develop guidance training objectives, course outlines, curriculum and training material by the end of the third quarter FY 2010, train the trainers and schedule training for the fourth quarter of FY 2010.

BASELINE OF FINANCIAL MANAGEMENT CAPABILITIES AND WEAKNESSES

Actions Taken

To drive and measure results, the Department identified and issued standard Key Control Objectives (KCOs) that:

- Capture the financial management capabilities and outcomes needed to achieve proper financial reporting.
- Serve as the baseline against which the effectiveness of financial controls can be evaluated.

- Mitigate risks and provide assurance that financial information is properly and accurately recorded and reported.
- Develop each Component's financial management capabilities baseline and use the KCOs to measure progress in eliminating weaknesses (i.e., ineffective controls).

The Department identified KCOs by using the GAO Financial Audit Manual (FAM) and coordinated them with the DoD IG. The Department is confident that it has established the most meaningful measure for developing a financial management capabilities baseline and for measuring and monitoring the correction of weaknesses that impede proper financial reporting.

The standard KCOs and related FIP requirements were included in the FIAR guidance. The guidance requires the Components to:

- Identify in their FIPs each KCO and whether each KCO has been assessed, and, if so, whether the control is weak or effective.
- During the Evaluation and Discovery and Corrective Action phases of the FIP, to assess internal controls to identify inherent risks and weaknesses in the processes designed to ensure the accuracy of financial information.
- If weaknesses are discovered, to include the required steps to remediate the control weakness and then to retest the control to ensure the control objectives are achieved.

The Components have modified their FIPs to include the required KCOs for the priority assessable units that presently are being worked for Wave 1, Wave 2 and Wave 3, and have begun to identify their progress in assessing the effectiveness of the KCOs. The KCO baselines are presented previous sections III and IV of this Report.

Planned Actions

The baseline of financial management capabilities and weaknesses based on KCOs will be more complete and accurately reflect the Components' status as they progress in assessing and evaluating their internal controls. In addition, the Department will strive to:

- Update the FIPs no less than monthly.
- Review and provide feedback to the Components on a monthly basis on their progress and the status of their KCOs.
- Present monthly progress reports to the OUSD(C), DCFO and FIAR Committee.
- Include the progress reports on the agenda for discussion and decision at quarterly FIAR Governance Board meetings.

The November 2010 FIAR Plan Status Report will provide the Department's progress against the baseline.

RESULTS-ORIENTED METRICS

Actions Taken

The Department has implemented two types of results-oriented metrics:

- Key Control Objective (KCO) and Key Supporting Documentation (KSD) Effectiveness Metrics – Capability Baseline
- Progress Metrics – Results-Oriented Metrics

Utilizing these two types of metrics, the Department monitors and reports the Components' progress in achieving the FIAR goals, objectives and priorities.

Each of the results-oriented metrics is explained below.

Key Control Objective and Supporting Documentation Effectiveness Metrics

The KCO and KSD Effectiveness Metrics track progress in achieving the end-state outcome of auditability. The KCO Effectiveness Metrics reflect the Components' progress in achieving a strong internal control program that ensures financial transactions are timely and accurately recorded.

The KCO Effectiveness Metrics provide management with visibility of the Components' assessment, testing and remediation activity until the KCOs have been determined to be effective. A standard set of KCOs are embedded in each of the Components' FIPs and have been linked to the discovery and corrective activities that identify them as either effective or a weakness.

KSD metrics capture the Components' progress in identifying supporting documentation deficiencies and problems that must be remediated before achieving auditability. Maintaining and making readily available acceptable evidential matter is critical to successful audits. This has been a long-standing deficiency in the Department and resolving it is essential. The FIAR methodology provides guidance to assist in resolving this impediment and this metric tracks progress.

The KCO and KSD Effectiveness Metrics for the SBR and existence and completeness priorities are provided in Sections III and IV of this Report.

Progress Metrics – Results-Oriented Metrics

The second type of metric is also results-oriented, but varies by assessable unit and tracks progress in accomplishing important objectives impacted by financial improvement activity. Example metrics include:

- Percent of inventory valued at moving average cost (MAC)
- Physical Inventory Variances
- Warehouse Refusal/Denial Rate
- Equipment Contracts Compliant with IUID

Progress Metrics for Military Equipment, Real Property, Inventory, Operating Materials and Supplies, and General Equipment are found in Section IV of this Report.

Planned Actions

The OUSD(C) is working with the OUSD(AT&L) and Components to identify and implement additional Progress Metrics. As the CMOs become more involved in the FIAR process, they will provide additional top-level assistance to identify additional metrics to monitor progress.

CHIEF MANAGEMENT OFFICERS' OVERSIGHT ROLE

Actions Taken

The DoD Chief Management Officer (CMO) and Military Department CMO positions have been filled. The oversight role of the CMOs was established in the NDAA for Fiscal Year 2008; however, the Department has developed more detailed responsibilities for the CMOs regarding their financial improvement role and responsibilities. The Military Department CMOs will:

- Coordinate and marshal resources from across the Department in support of the USD(C) financial improvement goals, objectives and priorities.
- Transform the budget, finance, accounting and human resource operations in a manner consistent with the comprehensive business transformation plan.
- Eliminate or reduce financial management systems that are inconsistent with the business systems architecture and transition plan.
- Ensure that the functional communities (e.g., Acquisition, Logistics) recognize their role in achieving audit readiness, since most financial transactions originate from business events in the functional community's business operations. The Department has worked for years to fully engage the functional communities in addressing auditability with varying success, but with the assistance of the Military Department CMOs, this will improve.

- Provide the unifying support needed to ensure that business system modernizations (e.g., ERPs) are fully linked with Component financial improvement activities. To date, linking these two important initiatives has been difficult because of the compartmentalized nature of the two different efforts.
- Participate as key members of the FIAR Governance Board. Chaired by the USD(C) and comprised of the Department's most senior financial management leaders, this board provides a forum for collaborative decisions impacting the FIAR goals, objectives, priorities, and strategy. The Board also monitors progress and assists in ensuring key milestones are achieved. In addition, the Board resolves cross-Component issues and provides a forum for sharing lessons learned, which is expected to be very useful as more financial statement audits are started and challenges identified and solutions identified.

Planned Actions

The Department will continue to engage the CMOs and DCMOs in the FIAR process through their participation in the FIAR Governance Board, described in section I of this Report.

ACCOUNTABILITY FOR FIAR ACTIVITY

Actions Taken

Accountability for improvement activity starts in the Office of the Under Secretary of Defense (Comptroller).

The performance standards of key individuals contain objectives for leading and accomplishing the Department's FIAR goals. These individuals include:

- Deputy CFO,
- FIAR Director,
- FIAR Directorate staff members, and
- Individuals throughout the DoD Components with responsibilities for achieving FIAR goals.

Linking performance to the Department's financial improvement goals and objectives is an important step the Department is taking to drive progress and achieve audit readiness.

As required by the FIAR guidance and FIP template, the Components identify the names of individuals and organizations that are accountable for discovery, assessment, testing, and corrective actions. This is another step that is driving accountability throughout the Department, in this case to each Component and office charged with improving financial information.

For the assessable units the SBR and existence and completeness priorities, which are areas where the Component FIPs are most up to date, the accountability fields have been updated to identify the responsible people and organizations.

Planned Actions

As the Components continue updating their FIPs, the FIAR Directorate will continue reviewing them and providing feedback to the Components. Included in such reviews are the accountability fields in the FIPs.

FIAR RESOURCES

Actions Taken

Adequately resourcing/funding financial improvement requirements and activity across the Department has been a problem. Although the FIAR goals are important and a DoD priority, funding has been limited and regularly competes with other priority requirements. Some Components have been more successful than others in obtaining funds for financial improvement, which is reflected in the progress they have made.

To address this resource problem, during the FY 2011 budget process, the OUSD(C)/Program Budget, along with the Deputy CFO and FIAR Directorate:

- Worked with the Army and Air Force to identify FY 2011 financial improvement budget requirements, resulting in additional funding for Army and Air Force in FY 2011, and
- Are using the FIPs to capture FIAR resource information to support the budget process and to provide more visibility of FIAR resource requirements.

The Components are identifying resource requirements and resource commitments for tasks/improvement work in their FIPs. This information will highlight resource shortages or under funding and to compete for and justify additional resources.

The Navy and DLA had sufficient funds budgeted in their FY 2011 budgets for FIAR activity, and therefore, did not receive additional funding.

Planned Actions

As the Department prepares the November 2010 FIAR Plan Status Report, it will ensure that the Component updates to their FIPs accurately reflect their FIAR resource requirements in order to summarize and provide this information to the OUSD(C)/Program Budget for the FY 2012 budget process. This requirement will be emphasized at the FIAR Governance Board and FIAR Committee meetings during the fourth quarter of each fiscal year.

MILITARY INTELLIGENCE PROGRAMS AND AGENCIES

Actions Taken

The Military Intelligence Programs and Agencies have implemented an internal control audit readiness strategy in accordance with the FIAR guidance. This strategy is intended to address financial statement and internal control concerns covering all National Intelligence Programs and includes audit readiness efforts as overseen by a level of governance to also involve a validation strategy and corrective action plan process. The strategy progresses from internal control preparation, validation and achieving financial excellence through processes, systems and people.

Within the DoD, there are four intelligence agencies (National Reconnaissance Office (NRO), Defense Intelligence Agency (DIA), National Security Agency (NSA) and National Geospatial-Intelligence Agency (NGA). As of FY 2009, only NRO has received an unqualified audit opinion. The remaining three agencies have yet to be audited; however, they anticipate material weaknesses would be reported if an audit was performed today. The implementation of the audit strategy is expected to resolve weaknesses for all components.

Planned Actions

Upon execution of the internal control audit readiness strategy, the following areas will be achieved:

- Focus groups will work to resolve audit impediments and accelerate Components' internal control projected audit readiness timeliness. These groups will evaluate internal controls, best practices, standard processes, baseline metrics, legacy data cleanup, data standardization and financial management guidelines.
- Approximately 80 percent of material weaknesses will be cleared through the strategy's guided procedures, with remainder cleared at each agency's pace.
- The Components will implement financial improvements and validate them using an audit readiness validation process to ensure controls are effective and balances are reconciled before undergoing an audit.
- The Components will evaluate internal control unique business operations on a case-by-case basis to evaluate the proper application of federal generally accepted accounting principles.
- Internal control progress will be tracked through quarterly corrective action plan submissions, baseline metrics, and financial statement reporting.

Appendix 3. Statement of Budgetary Resources Composition

Reporting Entities	Budgetary Resources*		Percent of Total
Under Audit			
Military Retirement Fund	$	50,303,962,635	4.27%
U.S. Army Corps of Engineers - Civil Works	$	40,394,543,982	3.43%
U.S. Marine Corps, GF	$	38,391,004,750	3.26%
TRICARE Management Activity - CRM	$	14,268,323,055	1.21%
Medicare-eligible Retiree Healthcare Fund	$	8,290,649,170	0.70%
Defense Commissary Agency	$	7,655,363,185	0.65%
Defense Finance and Accounting Service	$	1,600,708,030	0.14%
Defense Contract Audit Agency	$	501,701,746	0.04%
Office of the Inspector General, DoD	$	318,440,862	0.03%
Subtotal Under Audit	**$**	**161,724,697,416**	**13.73%**
Preparing for Audit			
Army, GF	$	320,490,685,931	27.20%
Air Force, GF	$	201,591,287,902	17.11%
Navy, GF	$	185,530,753,342	15.75%
Military Retirement Fund Payment	$	65,530,000,000	5.56%
Defense Logistics Agency, WCF	$	38,007,067,441	3.23%
Navy, WCF	$	29,024,958,565	2.46%
DoD Component Level Accounts	$	27,630,141,514	2.35%
Service Medical Activity	$	21,085,592,983	1.79%
Army, WCF	$	18,718,420,062	1.59%
Office of the Secretary of Defense	$	17,898,445,770	1.52%
Air Force, WCF	$	11,611,967,179	0.99%
U.S. Special Operations Command	$	11,515,699,390	0.98%
Missile Defense Agency	$	9,684,128,234	0.82%
Air Mobility Command	$	9,384,961,552	0.80%
Other 97 Funds Provided to the Army by OSD	$	5,718,523,836	0.49%
Defense Information Systems Agency, WCF	$	5,556,128,764	0.47%

Reporting Entities	Budgetary Resources*		Percent of Total
Preparing for Audit - *continued*			
Defense Advanced Research Projects Agency	$	4,630,405,349	0.39%
DoD Education Activity	$	3,398,056,969	0.29%
TMA - (FOD)	$	2,618,643,987	0.22%
Defense Information Systems Agency, GF	$	2,600,758,230	0.22%
Military Surface Deployment & Distribution	$	2,590,281,123	0.22%
Chemical Biological Defense Program	$	2,317,164,642	0.20%
Defense Security Cooperation Agency	$	1,705,910,466	0.14%
Defense Threat Reduction Agency	$	1,542,102,738	0.13%
Defense Contract Management Agency	$	1,284,093,209	0.11%
Defense Logistics Agency, GF	$	1,124,337,523	0.10%
Defense Technical Information Center	$	1,044,309,843	0.09%
U. S. Marine Corps, WCF	$	994,114,351	0.08%
Subtotal Preparing for Audit	**$**	**1,004,828,940,894**	**85.29%**
Immaterial Reporting Entities	**$**	**11,541,410,258**	**0.98%**
Total	**$**	**1,178,095,048,568**	**100.00%**

* *Source of dollar amounts from Line 7 of the FY 2009 Statement of Budgetary Resources.*

Appendix 4. Commonly Used Acronyms

Acronym	Definition
APSR	Accountable Property System of Record
AT&L	Acquisition, Technology, and Logistics
BTA	Business Transformation Agency
CFO	Chief Financial Officer
CMO	Chief Management Officer
CRM	Customer Resource Management
DBSMC	Defense Business Systems Management Committee
DCAA	Defense Contract Audit Agency
DCFO	Deputy Chief Financial Officer
DEAMS	Defense Enterprise Accounting Management System
DeCA	Defense Commissary Agency
DFAS	Defense Finance and Accounting Service
DLA	Defense Logistics Agency
DoD	Department of Defense
DoD OIG	Department of Defense Inspector General
DON	Department of the Navy
E&C	Existence and Completeness
EBS	Enterprise Business System
ECSS	Expeditionary Combat Support System

Acronym	Definition
ERP	Enterprise Resource Planning
ETP	Enterprise Transition Plan
FASAB	Federal Accounting Standards Advisory Board
FBWT	Fund Balance with Treasury
FFMIA	Federal Financial Management Improvement Act
FIAR	Financial Improvement and Audit Readiness
FIAR-PT	Financial Improvement and Audit Readiness Planning Tool
FIP	Financial Improvement Plan
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
GAGAS	Generally Accepted Government Auditing Standards
GAO	Government Accountability Office
GCSS	Global Combat Support System
GF	General Fund
GFEBS	General Fund Enterprise Business System
I&E	Installations and Environment
IPA	Independent Public Accountant or Independent Public Accounting Firm
IUID	Item Unique Identification

Acronym	Definition
LMP	Logistics Modernization Program
KCO	Key Control Objective
KSD	Key Supporting Documentation
MAC	Moving Average Cost
MERHCF	Medicare-Eligible Retiree Health Care Fund
NDAA	National Defense Authorization Act
OIG	Office of the Inspector General
OM&S	Operating Materials and Supplies
OMB	Office of Management and Budget
OSD	Office of the Secretary of Defense
OUSD(AT&L)	Office of the Under Secretary of Defense (Acquisition, Technology, and Logistics)

Acronym	Definition
OUSD(C)	Office of the Under Secretary of Defense (Comptroller)
RPAR	Real Property Acceptance Requirements
RPIR	Real Property Inventory Requirements
SBR	Statement of Budgetary Resources
TMA	TRICARE Management Activity
TMA-CRM	TRICARE - Contract Resource Management
USACE	United States Army Corps of Engineers
USD	Under Secretary of Defense
USD(AT&L)	Under Secretary of Defense (Acquisition, Technology, and Logistics)
USD(C)	Under Secretary of Defense (Comptroller)
USMC	United States Marine Corps