

FINANCIAL IMPROVEMENT AND AUDIT READINESS (FIAR) PLAN STATUS REPORT



MAY 2014

UNITED STATES DEPARTMENT OF DEFENSE

OFFICE OF THE UNDER SECRETARY OF DEFENSE (COMPTROLLER)/CHIEF FINANCIAL OFFICER

Table of Contents

Message from the Under Secretary of Defense (Comptroller)	iii
Messages from the Military Departments	v
Executive Summary	1
I. Statement of Budgetary Resources (Waves 1 & 2) by September 30, 2014	11
II. Mission Critical Assets Existence and Completeness (Wave 3) by June 30, 2016	17
III. Full Financial Statements (Wave 4) by September 30, 2017.....	23
IV. Service Provider Audit Readiness	27
V. Enterprise Resource Planning Systems.....	29
Appendix 1. Acronyms	A-1

The FIAR Plan Status Report was prepared in accordance with section 1003 of the National Defense Authorization Act (NDAA) for Fiscal Year (FY) 2010, as amended by the FY 2011, FY 2012, FY 2013, and FY 2014 NDAA's. The Report addresses issues impeding the reliability of the Department of Defense financial statements and serves as the Department's annual Financial Management Improvement Plan, required by section 1008(a) of the NDAA for FY 2002.

Preparation of this Report cost the Department of Defense an approximate total of \$74,500.

Message from the Under Secretary of Defense (Comptroller)/ Chief Financial Officer

The intense efforts of the last five years have led to significant progress toward improving financial information in the Department of Defense (DoD) and achieving auditable financial statements. Last December, the Marine Corps achieved a clean opinion on the current year of its budget statement—a major achievement and a first among the Department's Military Services. Many other Services and defense organizations have clean opinions or have made progress on key parts of their financial statements. By September 30, 2014, the goal set by law, I expect that most DoD budget statements will be audit ready. We will then begin the audit in a cost-effective manner, starting with the all-important current year of the budget statement.

The Department is also focusing on achieving audit readiness on statements identifying counts and locations of assets, known as existence and completeness. Our goal is to achieve audit readiness in this area by June 30, 2016. We are also planning to meet the September 30, 2017, goal to have all of the Department's financial statements ready for audit. The messages from the Chief Management Officers of the Military Departments, which follow, reaffirm our collective commitment to meeting these audit readiness goals.

One of the reasons I believe we will succeed in this effort is sustained leadership commitment. Secretary Hagel and the Service Secretaries remain fully committed to our audit goals, as do other pivotal senior leaders in the Department. As my tenure as the Department of Defense Chief Financial Officer draws to a close, our significant progress and strong leadership commitment leave me feeling confident the Department will succeed in improving financial information and achieving auditable financial statements.



A handwritten signature in dark ink, reading "Robert F. Hale".

Robert F. Hale
Under Secretary of Defense (Comptroller)/
Chief Financial Officer

This Page Left Blank Intentionally

Message from the Department of the Army Under Secretary and Chief Management Officer

Consistent with the National Defense Authorization Act of FY 2013, most of the Army is well-postured to achieve audit readiness of the schedule of budgetary activity by September 30, 2014, without an unaffordable or unsustainable level of one-time fixes and manual work-arounds and without delaying full auditability of the Army's financial statements by September 30, 2017.

We continue to make improved financial operations a top priority in the Army even as we face great challenges from the strain of war, the reduction of defense budgets, and furloughs. Our plan is sufficiently resourced and has the full support of the Army's top leaders. We regularly assess our progress and provide scorecards to pinpoint areas requiring additional focus. The significant commitment from our Soldiers and civilians enabled us recently to achieve several critical milestones, including receiving a positive audit opinion from the DoD IG on three major missile programs; successfully auditing more than half of the Army's real property; and undergoing our third mock audit of the Army's budgetary execution processes within GFEBS, the Army's new business system. Further, we continue to improve our business processes and enhance our Enterprise Resource Planning systems to include new logistics and personnel systems and more effective internal controls.

Perhaps the single most important thing we can do to achieve our financial management goals is to prepare our staff. Sufficiently trained personnel are critical to sound business operations in an organization as large and complex as the Army. We have trained more than 21,000 Army personnel in audit readiness fundamentals and continue to expand our online training resources and suite of audit readiness resources. I am extremely proud of our personnel and all they do to be Army Strong.



A handwritten signature in blue ink that reads "Brad R. Carson".

Brad R. Carson
Under Secretary and Chief Management Officer
Department of the Army

This Page Left Blank Intentionally

Message from the Department of the Navy Chief Management Officer

The Department of the Navy continues to demonstrate progress on its journey to full financial statement auditability as we prepare to complete our first Congressional mandate of asserting audit readiness for the Schedule of Budgetary Activity (SBA). First, the United States Marine Corps (USMC) received an unqualified (favorable) audit opinion for its FY 2012 SBA – a first for any military service. The DON has learned valuable lessons from the USMC audit and is incorporating these insights into the DON's overall strategy. Secondly, the DON has asserted nine out of the ten business areas composing the SBA, including recent assertions of Military Standard Requisitioning and Issue Procedures and Contract/Vendor Pay.

The significant progress the DON has made towards audit readiness can be attributed to the hard work and dedication demonstrated by managers and staff across the enterprise. They have worked tirelessly to reform business processes, increase financial accountability, embody good financial stewardship and improve how we do business in support of the warfighters. While the DON has demonstrated successes in audit readiness, there is more work required to sustain progress and to address the remaining challenges for full financial statement auditability.

Our efforts continue towards achieving audit readiness of the Schedule of Budgetary Activity by September 30, 2014 and full auditability of the Navy's financial statements by September 30, 2017 as mandated by the National Defense Authorization Act of FY 2013.



A handwritten signature in dark ink, appearing to read 'Thomas W. Hicks'.

Thomas W. Hicks
Performing the Duties of the
Under Secretary of the Navy

This Page Left Blank Intentionally

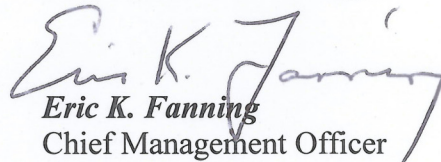
Message from the Department of the Air Force Chief Management Officer

The Department of the Air Force is fully committed to achieving and sustaining audit readiness. Our efforts have been substantial and include a wide spectrum of Air Force activities to reach these goals. However, as we continue to assess our readiness and design, implement, and test corrective actions, we believe a concerted effort and laser focus will be required in order for us to meet the 2014 deadline.

Over the last six months, the Air Force Financial Improvement and Audit Readiness (FIAR) team made substantial progress conducting auditability assessments of our Schedule of Budgetary Activity (SBA), and we are confident we will complete these assessments by the end of the third quarter of fiscal year 2014. Thanks to our ongoing discovery efforts, we have identified a substantial number of deficiencies and auditability impediments and are developing and implementing the necessary corrective actions, some of which will involve significant remediation activity. Results of the recent exams conducted on our civilian pay and funds distribution processes by an Independent Public Accountant have underscored the value of our strategy of getting auditors' eyes on our processes. As a result of these engagements, our resources are increasingly focused on remediating specific deficiencies that entail changes to our business processes, systems and our people's roles and responsibilities. Strengthening our financial systems, and the associated controls around those systems, remains our most critical challenge. Despite this challenge, the Air Force believes we will benefit greatly from an audit of our SBA in 2015, and further delays would place our goal of being ready for a full financial statement audit in 2017 at risk.

The Air Force is committed to becoming audit ready and our efforts to meet the 2014 deadline will continue up to the very last minute. I have determined the Air Force remains on a well-designed, albeit risky path to achieve audit readiness for the SBA by September 30, 2014, without an unaffordable or unsustainable level of one-time fixes and manual work-arounds and without delaying full auditability of our financial statements by September 30, 2017. Despite the risks inherent in our 2014 schedule, we are well on the path to achieving full audit readiness by 2017.




Eric K. Fanning
Chief Management Officer
Department of the Air Force

This Page Left Blank Intentionally

Executive Summary

The Department of Defense (DoD) is committed to achieving the audit readiness goals established by the Secretary of Defense and required by Congress. The Department's senior leaders are closely monitoring progress, addressing challenges, and focusing people and resources on the work needed to accomplish the goals on time. The Financial Improvement and Audit Readiness (FIAR) audit readiness goals are:

- September 30, 2014, for the General Fund Statement of Budgetary Resources (SBR)
- June 30, 2016, for existence and completeness of mission critical assets
- September 30, 2017, for all DoD financial statements

With a little more than four months remaining to accomplish the first goal of audit readiness for the budgetary financial statements, the Department is aggressively working to complete corrective actions. It is expected that most DoD budgetary financial statements will be audit ready by September 30, 2014. The Department will then begin audits of the FY 2015 budgetary statements in a cost-effective manner, beginning with the very important current-year budgetary information. The Department is also pursuing the other two goals.

FIAR STRATEGY

The FIAR Strategy groups individual end-to-end processes into four waves of sequential but interrelated activity:

Wave 1 – Appropriations Received Audit Readiness

Wave 2 – Statement of Budgetary Resources Audit Readiness

Wave 3 – Mission Critical Assets Existence and Completeness Audit Readiness

Wave 4 – Full Financial Statements Audit Readiness

Figure ES-1. FIAR Strategy and Timeline

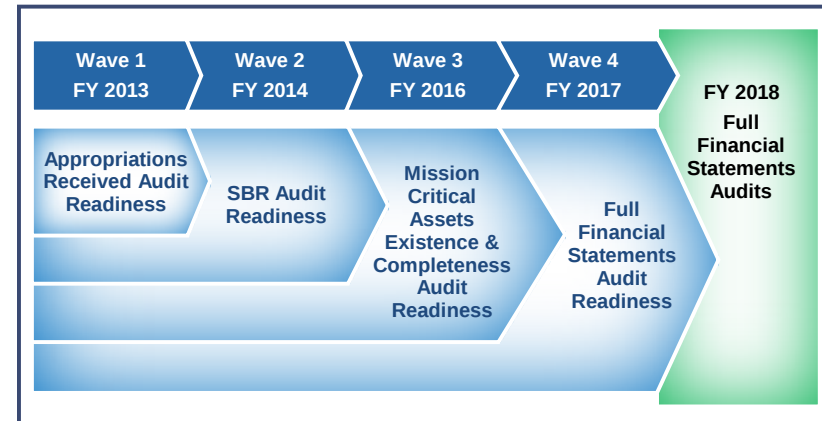


Figure ES-1 shows the four waves of the FIAR Strategy and the fiscal year when each wave will be completed. This strategy ensures coverage of all financial statements. Successful completion of the four waves leads to achieving interim audit readiness milestones, and ultimately, results in achieving a full-scope financial statement audit.

The Department has completed audit readiness for Wave 1, Appropriations Received. Because much of the work in Waves 1, 2, and 3 satisfy Wave 4 audit readiness requirements, Figure ES-1 shows all waves starting at the same time. However, the Components were directed to focus their FIAR work on the first three waves and will begin executing Wave 4 activities in FY 2015.

SIGNIFICANT PROGRESS TO DATE

The Department tracks audit readiness progress through financial statement audit opinions, audit readiness validated by DoD Office of the Inspector General (DoD OIG) or IPA examinations, and audit readiness assertions. Substantial progress is being made.

U.S. Marine Corps

Since the November 2013 FIAR Plan Status Report, the DoD OIG issued an unmodified or “clean” opinion on the audit of the U.S. Marine Corps FY 2012 Schedule of Budgetary Activity (SBA). The Marine Corps is the first DoD Military Service to receive an unmodified audit opinion. This significant accomplishment demonstrates a Military Service can achieve audit readiness and validates the sensible, cost-effective approach the Department is taking to achieve SBR audit readiness.

Audit Opinions on Financial Statements

To date, six other DoD organizations have received unmodified audit opinions on their FY 2013 financial statements, and one DoD organization received a modified opinion. Components that have not achieved full audit readiness will build on the audit readiness momentum and progress from Waves 1, 2, and 3 and the lessons learned from undergoing SBA audits.

Figure ES-2 lists the DoD Components that achieved audit opinions on their FY 2013 financial statements.

Figure ES-2. Financial Statement Audit Opinions

FY 2013 Unmodified Audit Opinions
U. S. Army Corps of Engineers – Civil Works
Defense Commissary Agency
Defense Contract Audit Agency
Defense Finance and Accounting Service
Defense Health Agency – Contract Resource Management
Military Retirement Fund
FY 2013 Modified Audit Opinions
Medicare-Eligible Retiree Health Care Fund

Audit Readiness Examinations

The Department is also making substantial progress below the level of statement opinions. Since the November 2013 FIAR Report, audit readiness has been validated by examination for:

- Army – Real Property at 23 installations

Four service providers have sustained and validated audit readiness through annual examinations for:

- Acquisition Technology and Logistics – Defense Property Accountability System
- Defense Civilian Personnel Advisory Service – Civilian Pay
- Defense Finance and Accounting Service – Civilian Pay, Military Pay, and Standard Disbursing Service
- Defense Information Systems Agency – Enterprise Computing Services

Additional examinations are underway for:

- Army – Fund Balance with Treasury
- Navy – Fund Balance with Treasury, Military Pay, Reimbursable Work Orders – Acceptor, and Reimbursable Work Orders – Grantor
- Defense Contract Management Agency – Contract Pay
- Defense Finance and Accounting Service – Contract Pay and Financial Reporting
- Defense Logistics Agency – Defense Agencies Initiative, Defense Automatic Addressing System/Global Exchange, Defense Travel System, and Wide Area Work Flow

FIAR Plan Status Report

Audit Readiness Assertions

Since the November 2013 FIAR Report, numerous assessable units have been asserted as audit ready. The Office of the Under Secretary of Defense (Comptroller) (OUSD(C)) reviews of new assertions underway are:

- Army – Personal Property (Medical Equipment and General Equipment)
- Navy – Contract/Vendor Pay and Military Standard Requisition and Issue Procedures
- Air Force – Capitalized Medical Equipment
- Chemical Biological Defense Program – Contract Pay and Reimbursable Work Orders – Grantor
- Defense Advanced Research Projects Agency – Civilian Pay, Contract Pay, Reimbursable Work Orders – Acceptor, Reimbursable Work Orders – Grantor, and Vendor Pay
- Defense Contract Management Agency – Civilian Pay, Contract/Vendor Pay, Reimbursable Work Orders – Acceptor, and Reimbursable Work Orders – Grantor
- Defense Health Agency – Civilian Pay, Contract Pay, Reimbursable Work Orders – Grantor, and Vendor Pay
- Defense Threat Reduction Agency – Civilian Pay, Contract Pay, Reimbursable Work Orders – Acceptor, Reimbursable Work Orders – Grantor, and Vendor Pay
- DoD Education Activity – Civilian Pay, Contract Pay, Reimbursable Work Orders – Acceptor, Reimbursable Work Orders – Grantor, and Vendor Pay
- Missile Defense Agency – Civilian Pay, Contract Pay, Reimbursable Work Orders – Grantor, Travel Pay, and Vendor Pay
- Service Medical Activity (Army, Navy, Air Force, National Capital Region Medical Directorate) – Civilian Pay, Consumables, Contract Pay, and Reimbursable Work Orders
- U.S. Special Operations Command – Civilian Pay and Contract Pay
- Washington Headquarters Service – Civilian Pay, Contract/Vendor Pay, and Reimbursable Work Orders – Grantor

Workforce Development

To help financial managers acquire skills and experience in crucial areas, including in financial audits, the Department has put in place a course-based financial management certification program. The DoD Financial Management Certification Program emphasizes appropriate training and development in major areas such as audit readiness, fiscal law, ethics, decision support, and leadership development. Three levels of certification outline training requirements in technical and leadership competencies. To date, the program has been implemented in 20 organizations with over 23,000 participants.

Additionally, the Department is delivering immediate, practical training on the importance of audit readiness to financial managers as well as to others who play a role. Nearly 27,000 certificates of training have been issued to attendees of live or online training offered by the OUSD(C) and the Department of the Army.

STATEMENT OF BUDGETARY RESOURCES (WAVE 2) BY SEPTEMBER 30, 2014

The Department expects most of its budget statement to be audit ready by September 30, 2014. Audit ready means the Department has strengthened internal controls and improved financial practices, processes, and systems so there is reasonable confidence the information can withstand an audit by an independent auditor. The Marines Corps has already asserted audit readiness and achieved a clean opinion on the current year of its budgetary statement. The

FIAR Plan Status Report

other Military Services expect to assert audit readiness of their budgetary statements by June 30, 2014, and many of the other Defense organizations (ODOs) asserted audit readiness in March 2014. Some additional ODOs will assert audit readiness in June 2014.

The Department is validating audit readiness in two ways. Where time permits, the Department has engaged an independent public accounting (IPA) firm to perform the validation. In other cases, the Department will rely on management to validate audit readiness by presenting the results of tests of internal controls, supporting documentation, and systems.

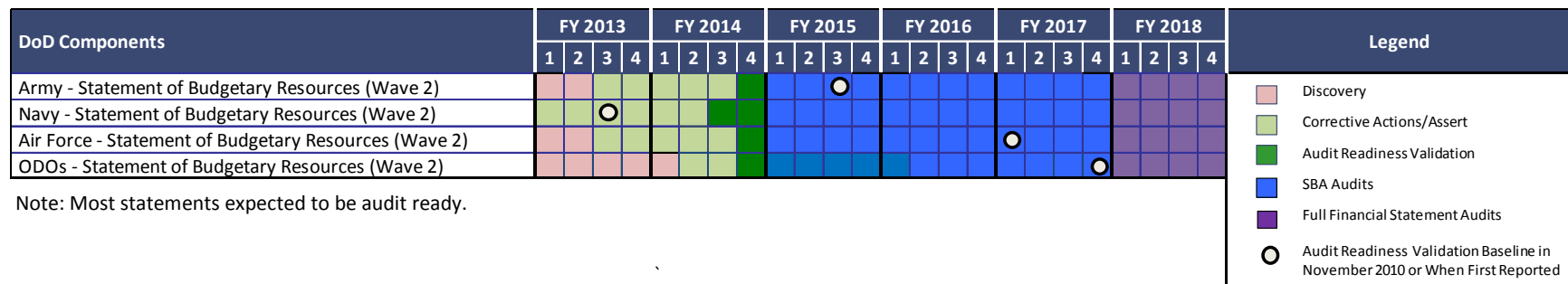
After validating audit readiness, the Department will proceed to audit of the FY 2015 budgetary statement in a cost-effective manner. As indicated in earlier FIAR Plan Status Reports, the Department will start the audits on current-year information contained in the Statement of Budgetary Resources, or SBR. The Department refers to current-year information of the SBR as the Schedule of Budgetary Activity, or SBA. Focusing first on the SBA reflects lessons learned from the Marine Corps audit of its SBR. The Marine Corps was unable to produce documentation supporting historical transactions associated with SBR opening balances quickly enough to meet the audit timelines. Historical documentation (e.g., requisitions,

receiving reports, and invoices) exists primarily in paper form and is dispersed across various commands and activities. The Marine Corps was, however, able to produce documentation for current-year transactions, which is the most important information to management and decision-makers.

To address this issue, the Department modified the FIAR Guidance to limit the scope of the first year FY 2015 SBR audits. The scope of the FY 2015 audits will be on current-year appropriation activity and transactions. The initial General Fund SBA audits will not include balances from prior year activity. As more accurate and audited data is accumulated, the Department will move toward an audit of the full SBR. This sensible approach has been favorably received by the Government Accountability Office (GAO) and the DoD OIG. SBA audits will continue for several years, when SBR audits will begin and include auditable opening balances from prior year SBA audits.

Figure ES-3 provides the status and plans for SBR audit readiness for the Military Departments and ODOs. As shown, all of the Components will complete audit readiness corrective actions in FY 2014, and SBA audits will begin in FY 2015. The first SBR audits will begin no later than FY 2018 as part of the Department's audit of its full financial statements.

Figure ES-3. General Fund SBR Audit Readiness and Planned SBA Audits (Wave 2)



MISSION CRITICAL ASSETS EXISTENCE AND COMPLETENESS (WAVE 3) BY JUNE 30, 2016

To ensure the Department's records and information systems used to manage assets are accurate and reliable, the Under Secretary of Defense (Comptroller)/Chief Financial Officer established audit readiness of existence and completeness of mission critical assets as a priority. Mission critical assets include:

- General Equipment (e.g., Ships, Aircraft, Combat Vehicles)
- Real Property
- Operating Materials and Supplies (OM&S)
- Inventory
- Internal Use Software

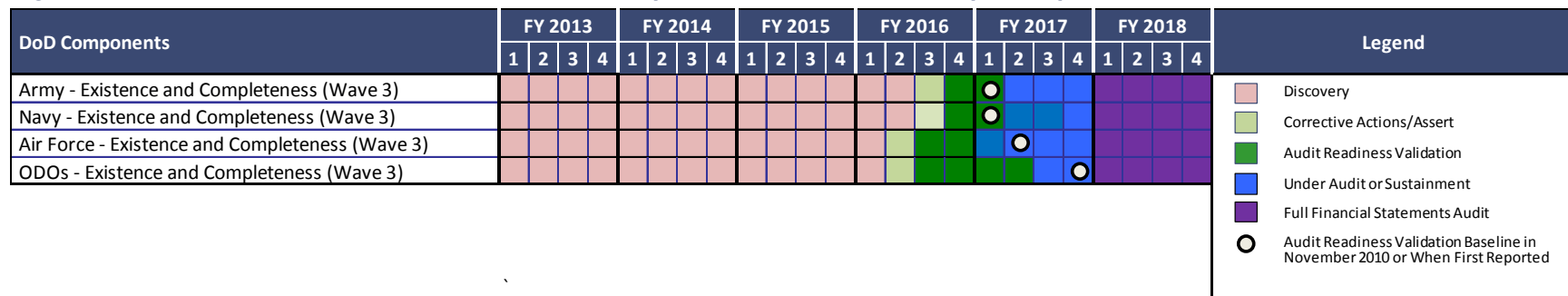
Resolving existence and completeness issues is an essential first step to valuing assets and reporting them on the Balance Sheet, which must be completed by September 30, 2017, to achieve audit readiness on DoD's full financial statements (Wave 4). Today, 69 percent of mission critical assets reported on the Balance Sheet as General Property, Plant, and Equipment have been asserted as audit ready, and 26 percent of mission critical assets reported as Inventory and Related Property have been asserted as audit ready.

Some of the more difficult mission critical assets remain to be made audit ready, such as the Department's significant quantities of OM&S. The Department owns over \$168 billion of OM&S, which is 19 percent of DoD tangible assets reported on the Balance Sheet.

OM&S comprises hundreds of thousands of different types of consumable items, some costing millions of dollars and some costing less than a dollar. OM&S includes spare and repair parts, ammunition, tactical missiles, aircraft configuration pods, and centrally-managed aircraft engines held for consumption. Regardless of dollar value, all OM&S items must be recorded in management systems and pass existence and completeness tests. As challenging as OM&S is to complete, the Components plan to achieve audit readiness by June 30, 2016.

Figure ES-4 provides the status and plans for the Military Departments and ODOs. Audit readiness activity will be completed in FY 2016, sustained in FY 2017 when valuation will be completed, and reported on the Department's FY 2018 financial statements.

Figure ES-4. Mission Critical Assets Existence and Completeness Audit Readiness (Wave 3)



FIAR Plan Status Report

Although Figure ES-3 shows completion of Wave 3 in FY 2016, existence and completeness of much of the Department's most critical assets' has been validated as audit ready, including:

- Army – over half of Real Property
- Navy – Ships, Aircraft, Trident Missiles, Satellites, Small Boats, OM&S – Ordnance, and OM&S – Uninstalled Aircraft Engines
- Air Force – Aircraft, OM&S – Cruise Missiles, OM&S – Aerial Targets and Drones, OM&S – Spare Engines, OM&S – Uninstalled Missile Motors, and Medical Equipment

FULL FINANCIAL STATEMENTS (WAVE 4) BY SEPTEMBER 30, 2017

Wave 4 includes all other General Fund financial statements and the Working Capital Fund financial statements, as well as related notes and supplemental information. Wave 4 also requires the Department to address challenging financial reporting areas such as Environmental Liabilities, and valuation of General Property, Plant, and Equipment; Inventory; and OM&S.

Detailed work plans for preparing for audits of DoD's full financial statements (Wave 4) have not been required of, or developed by, the Components. However, the FIAR Guidance was recently revised to support the Components' preparation of work plans for achieving full audit readiness for Wave 4, and work plans will be required in FY 2015.

Figure ES-5 provides a summary view of the Department's timeline for completing Wave 4 in FY 2017 and starting audits of DoD's full financial statements in FY 2018.

Figure ES-5. Full Financial Statements Audit Readiness (Wave 4)

DoD Components	FY 2013				FY 2014				FY 2015				FY 2016				FY 2017				FY 2018				Legend
	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	
Army - Full Financial Statements (Wave 4)																									
Navy - Full Financial Statements (Wave 4)																									
Air Force - Full Financial Statements (Wave 4)																									
ODOs - Full Financial Statements (Wave 4)																									

Corrective Actions/Assert

Audit Readiness Validation

Full Financial Statements Audit

Audit Readiness Validation Baseline in November 2010 or When First Reported

AUDIT READINESS CHALLENGES

Several factors and issues represent challenges that DoD must overcome.

Internal Controls

A strong and effective internal control environment is essential to achieving and sustaining audit readiness. To ensure a strong internal control environment is established and maintained, the FIAR Guidance requires audit readiness steps that focus on the internal controls within each business and financial process. Such steps include documenting and evaluating controls through testing, remediating deficiencies and weaknesses, and establishing periodic retesting. To assist the Components, the FIAR Guidance identifies the key financial reporting objectives for each business and financial process supporting the DoD financial statements. A large amount of time-consuming, tedious, and costly work remains to achieve and maintain an effective control environment across the Department.

The Department uses hundreds of business and financial information systems and micro-applications. Strengthening and ensuring effective application and general controls for these systems and applications is critically important to recording and reporting audit ready information and helps to minimize sample sizes, which are based on a percentage of all transactions. If auditors determine a system's controls are not effective, the sample size increases dramatically. Because of the huge volume of annual financial transactions, even a small percentage increase means a huge number of individual transactions. Sample sizes must be kept to a minimum if audits are to be completed in the time allowed and at a reasonable cost.

Beginning Balances

Correcting and supporting prior-year transactions in beginning balances is time consuming and costly. Regardless, this challenge must be overcome by September 30, 2017, when the Department's

full financial statements must be audit ready and include beginning balances.

The Department's strategy for preparing beginning balances for audit varies depending on the financial statement and line item. For the SBR, for example, the Department will develop auditable beginning balances over time using the SBA approach. The SBA approach will result in auditable beginning balances as soon as possible and no later than the FY 2018 SBR. For line items, such as General Property, Plant, and Equipment on the Balance Sheet, the FIAR strategy is to apply the most common-sense and cost-effective approach to developing audit ready beginning balances.

Asset Valuation

Federal accounting standards require tangible assets, such as ships, aircraft, buildings, spare parts, and supplies, to be valued and reported on annual financial statements. The Department owns nearly a trillion dollars (Net Book Value) in tangible assets located worldwide, and accurately reporting, as well as maintaining readily available and acceptable supporting valuation documentation, is a significant challenge. Asset valuation, even when using a relatively new federal accounting standard permitting the use of estimates, is a challenge. Some of the more challenging complexities include:

- Numerous configurations of highly complex military equipment and weapons systems
- Military equipment and weapons systems that have been modified, upgraded, or overhauled
- Renovated and improved real property assets that have changed in value since originally placed in service
- Large inventories of missiles, ammunition and munitions, spare engines, equipment parts, supplies, etc.
- Enormous quantities of deployed General Equipment, Inventory, and OM&S located in Afghanistan and worldwide

FIAR Plan Status Report

Additional complexities exist for identifying and valuing Internal Use Software and DoD property in the possession of contractors.

Adding to the challenge, most Property, Plant, and Equipment (PP&E) valuation (i.e., historical cost) information reported on the Balance Sheet is not used by DoD decision makers, as verified by a business case performed by the Department in 2011 at the direction of Congress. Nevertheless, the Department is planning to value PP&E assets in accordance with federal accounting standards, using cost effective approaches.

Achieving mission critical asset existence and completeness audit readiness will ensure accurate quantity and location information and support valuation activities. However, a significant amount of time consuming and costly work remains to be done to determine and document the value of the Department's assets.

FFMIA Compliance

The Department's hundreds of financial systems materially affect DoD financial statements. Financial systems include budget, accounting, and finance systems, as well as business feeder systems, such as personnel, logistics, and property systems, where most financial transactions originate. Although some systems are being replaced, many will still be in use after FY 2017 when the Department is required to produce auditable financial statements. Additionally, a significant number of systems do not comply with the Federal Financial Management Improvement Act (FFMIA) of 1996 (Public Law 104-208), which entails compliance with the U.S. Standard General Ledger and Treasury Financial Manual.

Implementation of the Department's Standard Financial Information Structure (SFIS) within DoD systems will enable better compliance with FFMIA. To further manage this challenge, the Department has identified systems that materially affect audit readiness and is collecting information on micro-applications. The OUSD(C) is working with the Deputy Chief Management Officer and the Office of the Secretary of Defense Chief Information Officer to ensure systems achieve FFMIA and SFIS compliance.

Human Capital

The Department needs to hire more experienced and qualified DoD employees to support audits of the SBA and full financial statements. Luring experienced CPAs from IPA firms into the DoD workforce, where salaries are often not comparable and annual cost of living pay raises nonexistent or minimal, has been difficult. Ongoing hiring freezes exacerbate this problem. To minimize this challenge until more CPAs can be hired, the Department is:

- Improving the DoD financial management workforce through the Financial Management Workforce Certification Program
- Providing specialized FIAR training courses
- Using mock audits and examinations to validate audit readiness of assessable units and give DoD employees experience in supporting financial statement auditors

Budgetary Turmoil

In recent years, budgetary turmoil has impeded audit readiness progress and caused many other serious problems. Budgetary challenges severely affect senior leadership time, civilian hiring, workforce morale, training, travel, and availability of funds. The challenges the Department faces to improve business and financial processes, controls, and systems is significant and complex without having to manage and overcome these additional impediments and challenges. The Department very much hopes the budget turmoil is a thing of the past. If it is not, the turmoil will continue to impede audit progress and cause many other problems.

LEADERSHIP COMMITMENT AND GOVERNANCE

Strong and highly visible leadership commitment and effective governance offset these challenges and are essential to FIAR success. Secretary Hagel has repeatedly emphasized his commitment to the audit effort and is regularly informed about the Department's FIAR plans and progress.

In February 2014, the Secretary hosted an event recognizing the Marine Corps for becoming the first DoD Service to achieve audit readiness and receive an unmodified opinion on its FY 2012 SBA. More than 75 past and present leaders gathered in the Pentagon's Hall of Heroes for the event. Nine DoD Agencies were also recognized for the substantial progress made in achieving and sustaining auditable financial statements.

The Military Department Secretaries and Chiefs of Staff of the Military Services are also committed to specific near-term goals that lead to auditable financial statements. Their commitment has been reinforced at the command-level, where mission activity triggers financial transactions and where internal controls must be effective.

Additionally, the Department has maintained a formal FIAR governance process comprising most of the Department's key senior political leaders, senior executives, and senior action officers, who attend regularly scheduled FIAR Governance Board, FIAR Committee, and FIAR Subcommittee meetings. At these meetings, senior leadership and Component representatives discuss audit readiness status, plans, issues, risks, and lessons learned.

AUDIT READINESS RESOURCES

Despite challenging budget times, substantial funds have been set aside and programmed to support achieving auditable financial statements. The FIAR activities funded by the amounts in Figure ES-6 include:

Audit Readiness, Validations, and Audits include resources for:

- Evaluation, discovery, and corrective actions of the Components and their service providers (e.g., Defense Finance and Accounting Service (DFAS)), and includes documenting and modifying processes and controls, identifying internal control deficiencies through testing and remediation of deficiencies, and evaluating transaction-level evidential matter and ensuring it is readily available.
- Activities to test or verify audit readiness after completing corrective actions and preparation of management assertions.
- IPA audit readiness validations and financial statement audits.

Financial Systems includes resources for designing, developing, and deploying an audit-ready systems environment such as resources to make needed and cost-effective changes to legacy systems that will be part of the systems environment. Financial System resources also include design, development, deployment, interfaces, data conversion and cleansing, independent verification and validation and testing, implementation of controls and control testing, and system and process documentation. Enterprise Resource Planning (ERP) systems deployment costs are not included.

Figure ES-6. DoD Audit Readiness Resources (Dollars in Millions)

	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Audit Readiness, Validations, and Audits	517.7	589.4	522.8	414.2	403.5	405.8
Financial Systems (not including ERPs)	106.6	89.7	76.8	77.9	66.0	30.1
Total Resources	624.3	679.1	599.6	492.1	469.5	435.9

This Page Left Blank Intentionally

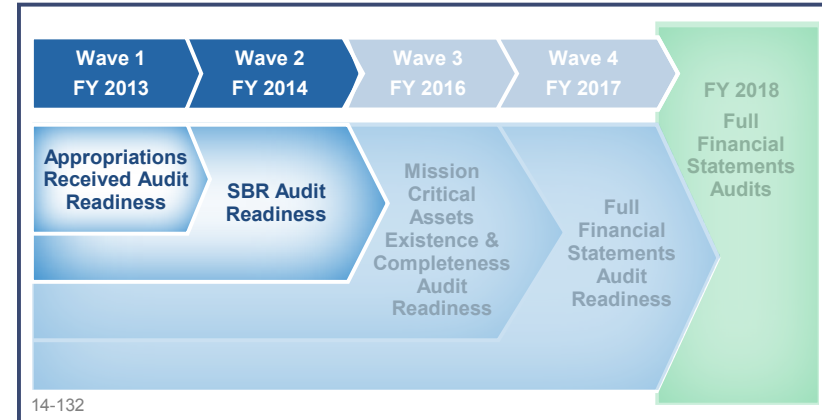
I. Statement of Budgetary Resources (Waves 1 & 2) by September 30, 2014

Waves 1 and 2 of the FIAR Strategy (Figure I-1) focus financial improvement activity on the information most often used to manage the Department: budgetary information reported on the SBR. Wave 1 addresses the processes, controls, and systems used to manage appropriations received and has been successfully completed. Wave 2 focuses improvement activity on the business and financial processes, controls, and systems used to obligate and outlay DoD funds, and audit readiness work will be completed by June 30, 2014.

By focusing improvement efforts on budgetary information and the SBR, the Department:

- Improves the visibility of budgetary transactions resulting in more effective use of resources
- Supports operational efficiencies through more readily available financial information
- Enhances fiscal stewardship by ensuring funds appropriated, expended, and recorded are reported accurately, reliably, and timely

Figure I-1. FIAR Strategy and Timeline



- Tightens budget processes and controls (e.g., precludes Antideficiency Act violations)

Figure I-2 provides a summary view of the Components' plans for completing Wave 2 SBR audit readiness and beginning SBA audits in FY 2015. SBA audits will continue through FY 2017. SBR audits will begin as soon as possible and no later than FY 2018.

Figure I-2. Wave 2 General Fund SBR Audit Readiness Status and Planned SBA Audits

DoD Components	FY 2013				FY 2014				FY 2015				FY 2016				FY 2017				FY 2018				Legend
	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	
Army - Statement of Budgetary Resources (Wave 2)																									
Navy - Statement of Budgetary Resources (Wave 2)																									
Air Force - Statement of Budgetary Resources (Wave 2)																									
ODOs - Statement of Budgetary Resources (Wave 2)																									

DiscoveryCorrective Actions/AssertAudit Readiness ValidationSBA AuditsFull Financial Statement AuditsAudit Readiness Validation Baseline in November 2010 or When First Reported

Note: Audits of the SBR will begin as soon as possible and no later than FY 2018, when full financial statement audits begin.

Note: Audits of the SBR will begin as soon as possible and no later than FY 2018, when full financial statement audits begin.

STATEMENT OF BUDGETARY RESOURCES AUDIT READINESS STATUS

As shown in Figure I-3, 78 percent of the Department is preparing for audits in FY 2015, and 22 percent has an audit opinion or is ready for audit. By June 30, 2014, it is expected that most of the Department, including the Military Departments, will have asserted audit readiness, meaning all material reporting entities will either have an audit opinion or be ready for audit.

Figure I-3. Status of DoD SBR Audit Readiness

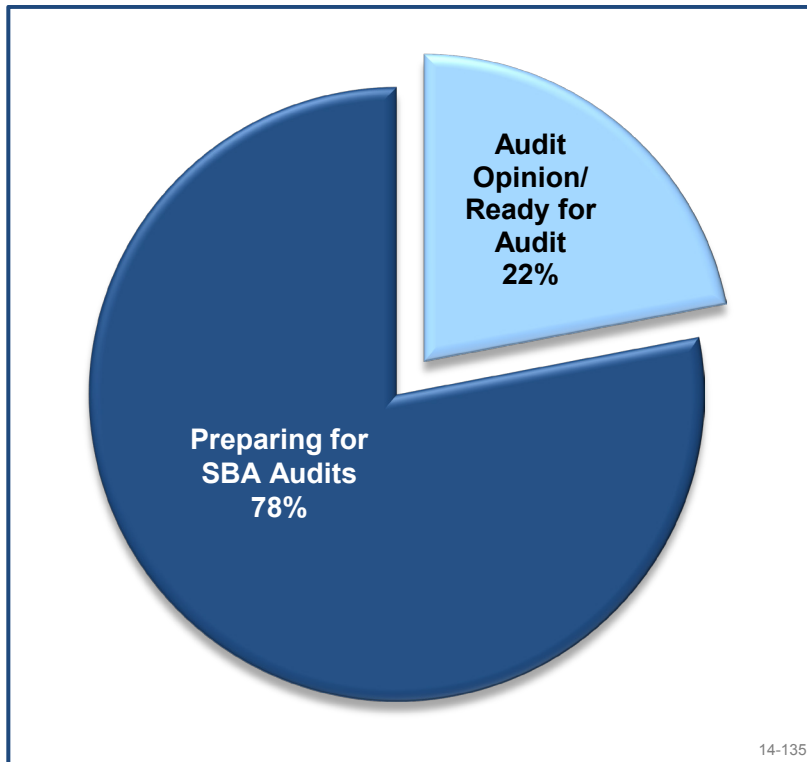


Figure I-4 shows the FY 2013 SBR budgetary resources by those Components that have an SBR audit opinion or are audit ready and by those preparing for audit. Figure I-3 graphs the dollar amounts and percentages.

Figure I-4. FY 2013 Budgetary Resources by Component

DoD Component	Budgetary Resources (\$ in Millions)	Percent
Audit Opinion/Audit Ready		
Military Retirement Fund	\$129,192	11.77
U.S. Army Corps of Engineers – Civil Works	30,279	2.76
U.S. Marine Corps	29,812	2.72
Defense Health Agency – Contract Resources Management	15,614	1.42
Medicare-Eligible Retiree Healthcare Fund	14,796	1.35
Defense Commissary Agency, Working Capital Fund	7,351	0.67
Defense Information Systems Agency, Working Capital Fund	6,362	0.58
Defense Information Systems Agency, General Fund	2,567	0.23
Defense Finance and Accounting Service	1,262	0.11
Defense Contract Audit Agency	614	0.06
DoD Office of the Inspector General	357	0.03
Defense Commissary Agency, General Fund	338	0.03
Subtotal	\$238,546	21.73
Preparing for SBA Audits		
Army, General Fund	\$266,478	24.27
Air Force, General Fund	187,769	17.10
Navy, General Fund	181,857	16.57
Defense Logistics Agency, Working Capital Fund	40,438	3.68
Navy, Working Capital Fund	31,820	2.90
DoD Component-Level Accounts	26,311	2.40
Service Medical Activity	21,346	1.94
U.S. Special Operations Command	12,286	1.12
Army, Working Capital Fund	13,661	1.24
Air Force, Working Capital Fund	10,966	1.00
Other Defense Components/Reporting Entities	66,313	6.04
Subtotal	\$859,245	78.27
Total Budgetary Resources	\$1,097,791	100.00

WAVE 1 – APPROPRIATIONS RECEIVED (VALIDATED AS AUDIT READY)

Wave 1 is the first step in receiving, recording, and tracking the funds appropriated to the Department to accomplish its mission. In August 2011, an IPA firm issued an unmodified opinion on Wave 1, Appropriations Received, for the Army, Navy, and Air Force. In FY 2013, the Department validated audit readiness of Appropriations Received for the ODOs thus completing Wave 1.

WAVE 2 – STATEMENT OF BUDGETARY RESOURCES (AUDIT READY BY SEPTEMBER 30, 2014)

The Department will complete General Fund SBR audit readiness by September 30, 2014, with an initial focus on current-year budgetary activity. Audit ready means the Department has strengthened internal controls and improved financial practices, processes, and systems so there is reasonable confidence the information can withstand an audit by an independent auditor.

Schedule of Budgetary Activity

The Marine Corps initiated audits of its FY 2010 and FY 2011 General Fund SBR but was unable to produce documentation supporting historical transactions associated with opening balances quickly enough to meet the audit timelines. After limiting the scope to current-year transactions, the Marine Corps successfully completed an audit of its FY 2012 Schedule of Budgetary Activity, or SBA. Based on lessons learned from the Marine Corps' SBR and SBA audits, the Department is limiting the scope of the FY 2015 audits to current-year budgetary activity reported in an SBA.

The SBA is a DoD financial schedule that presents a subset of activity or elements of the Department's SBR. The SBA presents budgetary and financial activity, including the receipt and execution of budgetary funding.

Similar to the SBR, the SBA comprises:

1. Budgetary Resources
2. Status of Budgetary Resources
3. Change in Obligated Balance
4. Budget Authority and Outlays, Net

The Department will begin preparing and undergoing SBA audits in FY 2015 on appropriations received in FY 2015. SBA audit readiness demonstrates the Department's procedures, processes, controls, and systems have been effectively improved and are capable of reporting materially complete and accurate financial and budgetary activity for current-year appropriations in accordance with generally accepted accounting principles (GAAP).

The first SBA audits in FY 2015 will not include prior year appropriations; however, each year will be sustained going forward. FY 2016 SBAs will include FY 2015 appropriations, and FY 2017 SBAs will include FY 2015 and FY 2016 appropriations. SBA audits will continue through FY 2017, and SBR audits will begin as soon as possible and no later than FY 2018. This cost-effective approach significantly reduces the amount of time and resources needed to prepare FY 2014 and other prior year appropriation information for audit, and helps to ensure FY 2018 SBR information is fully auditable. This approach has been favorably received by the GAO and DoD OIG.

SBAs will be audited in accordance with the American Institute of Certified Public Accountants Codification of Statements on Auditing Standards 805, *Special Considerations – Audits of Single Financial Statements and Specified Elements, Accounts, or Items of a Financial Statement*. The Army, Navy, Air Force, and ODOs are completing remaining financial improvement activities and establishing the infrastructure needed to support the SBA audits in FY 2015.

FIAR Plan Status Report

Remaining FY 2014 Audit Readiness Activity

Highlights of remaining improvement activities to be completed by September 30, 2014, in preparation for the SBA audits in FY 2015 for the Military Departments and ODOs include:

Army

- Complete corrective actions based on findings from an IPA examination of General Fund SBR processes, controls, and systems by June 30, 2014.
- Ensure legacy processes and systems are auditable to support an SBA assertion in advance of Integrated Personnel and Pay System – Army (IPPS-A) full deployment for military pay.
- Continue monthly Army-wide SBR audit readiness testing, including both internal control and substantive testing. Summarize and distribute results, trends, and recommendations to the commands.
- Assert SBA audit readiness by June 30, 2014.

Navy

- Work with the Budget Submitting Offices and service providers on the Financial Statement Compilation and Reporting assessable unit to complete corrective actions, ensure adequate supporting documentation for adjusting journal entries exists, and standardize close-out processes for financial period reporting.
- Complete remaining Federal Information System Controls Audit Manual (FISCAM) assessments and the standard systems documentation to support the SBA assertion. This includes testing information technology system controls, validating transaction data process flows and architecture documentation, and enhancing policies and procedures.
- Reconcile disparate feeder systems and general ledgers systems to demonstrate the completeness of transactions. Remaining

actions include improving the infrastructure and establishing the tools required to store, reconcile, and resolve identified discrepancies with business owners.

- Assert SBA audit readiness by June 30, 2014.

Air Force

- Make limited, cost-effective changes to legacy systems to address audit “dealbreakers” and complete corrective actions while continuing to deploy Air Force ERPs (Defense Enterprise Accounting and Management System (DEAMS) and Air Force Integrated Personnel and Pay System (AF-IPPS)).
- Refine the SBR Air Force Reconciliation Tool to identify variances in existing source system reconciliations and ensure all systems have been captured. The tool will enable the Air Force to capture the transaction universe.
- Identify, integrate, and address “handoff controls” (End User Controls) from service provider examination reports for inclusion in Air Force work products.
- Assert SBA audit readiness by June 30, 2014.

ODOs

Most of the ODOs asserted SBA audit readiness in March 2014, and other ODOs will assert by June 30, 2014. The OUSD(C) is reviewing the assertions to ensure the ODOs are ready for an SBA audit in FY 2015. Other activities include:

- Implement Department Reconciliation and Reporting Tool (DRRT) Fund Balance with Treasury reconciliation tool for ODO-level reconciliations and assert audit readiness on Fund Balance with Treasury and Financial Reporting by June 30, 2014.
- Test completed corrective actions, such as continual reconciliation of source systems to general ledgers, to ensure controls are in place and supporting documentation is available.

FIAR Plan Status Report

- Work with service providers to ensure results of Statement on Standards for Attestation Engagements (SSAE) No. 16 examinations, FISCAM reviews, and other activities support audit readiness, or implement necessary corrective actions.
- Remediate deficiencies identified during testing, SSAE No. 16 examinations, and FISCAM reviews of key information technology systems.

PLANS FOR SCHEDULE OF BUDGETARY ACTIVITY IN FYs 2015, 2016, 2017

In addition to the audit readiness work being completed by the Components, SBA audits require considerable planning and preparation by the OUSD(C), Components, and DoD OIG. Systems must be adapted to support the SBAs, an effective infrastructure to support hundreds of auditors is needed and must be in place to ensure cost-effectiveness and successful audits, an acquisition strategy developed and deployed to hire IPA firms, and a system for tracking and remediating audit findings stood up.

Producing Annual Schedules of Budgetary Activity

The OUSD(C) issued detailed guidance and instructions to the Components on the form and content of the SBAs to ensure the schedules are prepared in accordance with GAAP. The instructions specify the reporting entities and funds to be included (i.e., General Funds, Revolving Funds, Special Funds, Deposit Funds, and Trust Funds), what SBR information will be presented in the SBA, and how each year's budget activity (FY 2015 – FY 2017) will be presented. In addition, the instructions and guidance address preparing the accompanying Management's Discussion and Analysis and footnote disclosures.

The Department uses the Defense Departmental Reporting System – Audited Financial Statements (DDRS-AFS), operated by DFAS, to produce the annual DoD financial statements, including the SBR. However, DDRS-AFS presently does not have the capability to

routinely and consistently generate a standard and complete SBA for the Components. DFAS is modifying DDRS-AFS to enable producing Component SBAs quarterly and support SBA audits beginning in FY 2015. Modifications are projected to be completed in June 2014.

Establishing an Audit Support Infrastructure

The OUSD(C) and Components must be prepared and an infrastructure in place on the first day the auditors begin the SBA audits. Past years of DoD OIG and IPA audits and examinations of SBR assessable units have been a learning experience. Examples of requirements for implementing an effective infrastructure include:

- Having readily available detailed documentation for processes, controls, and systems, and SSAE No. 16 examination reports from service providers for shared processes.
- Maintaining the capability to reconcile reported SBA amounts to general ledgers, produce journal vouchers and supporting detailed information, and produce a complete universe of transactions.
- Supporting auditor transaction testing with the ability to provide transaction documentation within 48 hours.

Plans for establishing an adequate infrastructure within the OUSD(C) and each Component to support the SBA audits are being completed. While many of the individuals who have been working financial improvement activities will continue in that capacity through FY 2017, others will be dedicated to supporting the SBA audits.

Schedule of Budgetary Activity Audits to Be Conducted by the DoD OIG

Section 3512 of title 31, United States Code, as amended by the Chief Financial Officers Act of 1990, requires the financial statements of federal agencies to be audited by their respective

FIAR Plan Status Report

Inspector General or an independent external auditor, as determined by the Inspector General of the agency. Accordingly, the DoD OIG is responsible for the SBA audits to be conducted in FY 2015, but the DoD OIG does not have the staffing-level needed to conduct all of the required audits.

The Department is working with the DoD OIG to develop an acquisition strategy for employing IPAs to conduct the audits. Prior to hiring an IPA firm to conduct an SBA audit, the DoD OIG will review the Component's audit readiness assertion and, based on the assertion, perform a limited review of the Component's audit readiness. Only after the DoD OIG is assured of a Component's audit readiness will it execute a competitive contract to acquire the audit services of an IPA. The DoD OIG will hire the IPA firm, oversee the audit, and issue the resulting audit opinion.

Tracking and Remediating Audit Findings

The Department does not expect clean audit opinions on the initial SBA audits. Experience both within the Defense Department and at other federal agencies suggests auditors will likely find deficiencies and material weaknesses. When deficiencies and material weaknesses are identified, the auditors issue Notification of Findings and Recommendations (NFRs). Tracking the NFRs to ensure satisfactory and timely remediation is critical to meeting the goal of full financial statement audit readiness by September 30, 2017.

To facilitate tracking and managing the NFRs, the OUSD(C) developed a web-based system, the "NFR Tracker Tool," to capture and prioritize material weaknesses and significant deficiencies, and monitor corrective action plans. In addition to cataloging the NFRs, the NFR Tracker Tool captures:

- Action organization and status
- Management's response to recommendations
- Information systems affected

- Correction action information (e.g., key remediation activities, implementation dates, tested completion dates)

The tool went live in March 2014 and provides monthly and quarterly reports and metrics to OUSD(C).

PERCENTAGE OF STATEMENT OF BUDGETARY RESOURCES ASSERTED AS AUDIT READY AND UNDER AUDIT

The Department is tracking SBR audit readiness progress and reporting it within the FIAR governance process. Figure I-5 shows the audit readiness status for major line-items of the SBR.

Within the figure, asserted means that management has submitted an assertion to the OUSD(C) indicating all deal breakers have been met and the assessable unit, financial statement line-item, or financial statement is ready for audit. Audited means a DoD OIG led audit has been conducted on the applicable assessable unit, financial statement line-item, or financial statement and an unmodified or modified opinion was issued.

Figure I-5. Percentage of SBR Asserted and Audited

	Percent Asserted	Percent Audited
Appropriations Received	100	27
Obligations Incurred	42	23
Outlays	22	10

II. Mission Critical Assets Existence and Completeness (Wave 3) by June 30, 2016

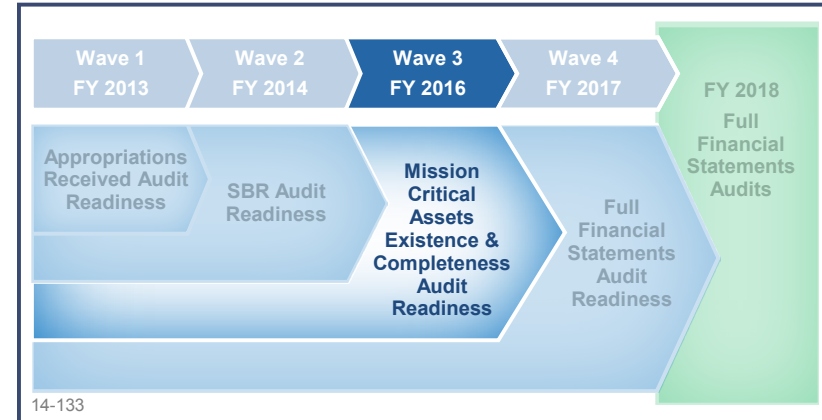
In FY 2013, the Department established a completion date of June 30, 2016, for Wave 3, Mission Critical Assets Existence and Completeness Audit Readiness (Figure II-1). Resolving existence and completeness issues is an essential first step to valuing and reporting assets on the Department's Balance Sheet. Balance Sheet categories of mission critical assets are:

- General Property, Plant, and Equipment
 - General Equipment (e.g., Ships, Aircraft, Vehicles)
 - Real Property
 - Internal Use Software
- Inventory and Related Property
 - Inventory
 - Operating Materials and Supplies

Audit readiness has been achieved on 69 percent of General Property, Plant, and Equipment and on 26 percent of Inventory and OM&S. The benefits to management include:

- Increased transparency and visibility of DoD assets
- Improved logistics supply chain and inventory systems, which ensure that items needed by the warfighter are available when needed and not procured unnecessarily
- Improved ability to acquire, maintain, and retire assets in a timely manner
- Better quality management information
- Stronger control over assets, preventing misuse, theft, or loss

Figure II-1. FIAR Strategy and Timeline



AUDIT READINESS STATUS AND PLANS

In achieving audit readiness on Wave 3, the Components assert that:

- All assets recorded in the Accountable Property Systems of Record (APSRs) exist (Existence)
- All existing assets are recorded in the APSRs (Completeness)
- The Component has the right (Rights) to report the assets
- Assets are consistently categorized, summarized, and reported from period to period (Presentation and Disclosure)

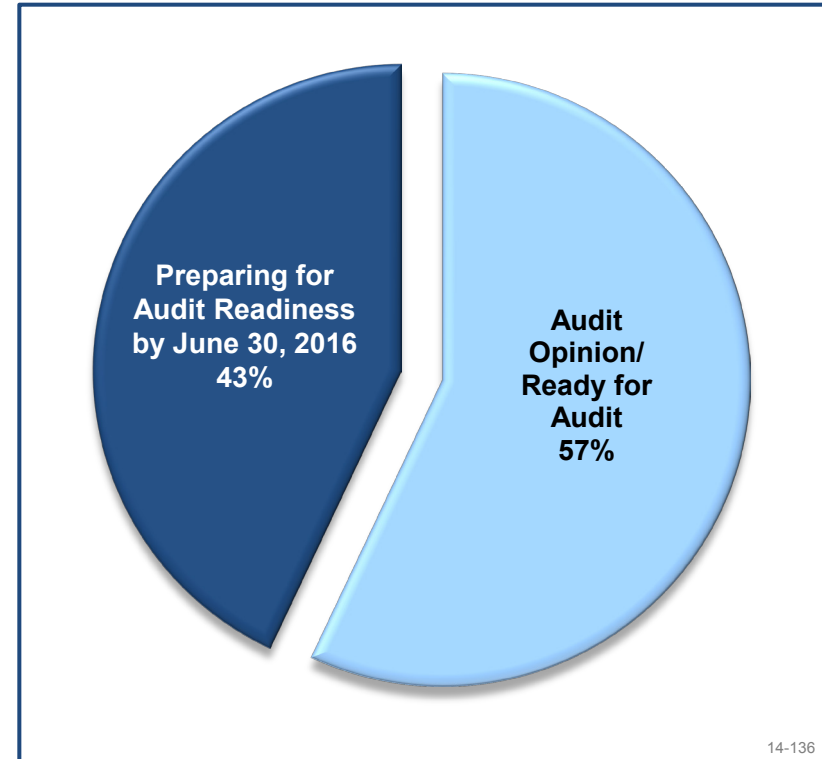
In January 2014, the Department expanded mission critical assets existence and completeness audit readiness to include improving Internal Use Software financial reporting information. Internal Use Software must be reported on the Department's Balance Sheet, and the Components are working with the information technology communities to develop detailed financial improvement plans.

FIAR Plan Status Report

Figure II-2 shows the cumulative status of mission critical assets existence and completeness audit readiness. As indicated, 57 percent of the Department's mission critical assets either have an audit opinion or have been asserted as audit ready, and 43 percent will be audit ready by June 30, 2016. The Army, Navy, and Air Force have asserted audit readiness on the majority of their most important mission critical assets:

- Army
 - AH-64A Apache, AH-64D Apache Longbow, UC-35A Utility Aircraft, CH-47F Improved Cargo Helicopter, OH-58D Aerial Scout Helicopter, UH-60L and UH-60M Blackhawk Utility Helicopters, and UH-72A Light Utility Helicopter
 - Real Property at 23 Installations
- Navy
 - Ships and Submarines
 - Aircraft
 - Trident Missiles
 - Satellites
 - Uninstalled Aircraft Engines
 - Ordnance
- Air Force
 - Intercontinental Ballistic Missiles
 - Satellites
 - Aircraft
 - Cruise Missiles
 - Aerial Targets and Drones
 - Spare Engines
 - Uninstalled Missile Motors

Figure II-2. Mission Critical Assets Existence and Completeness



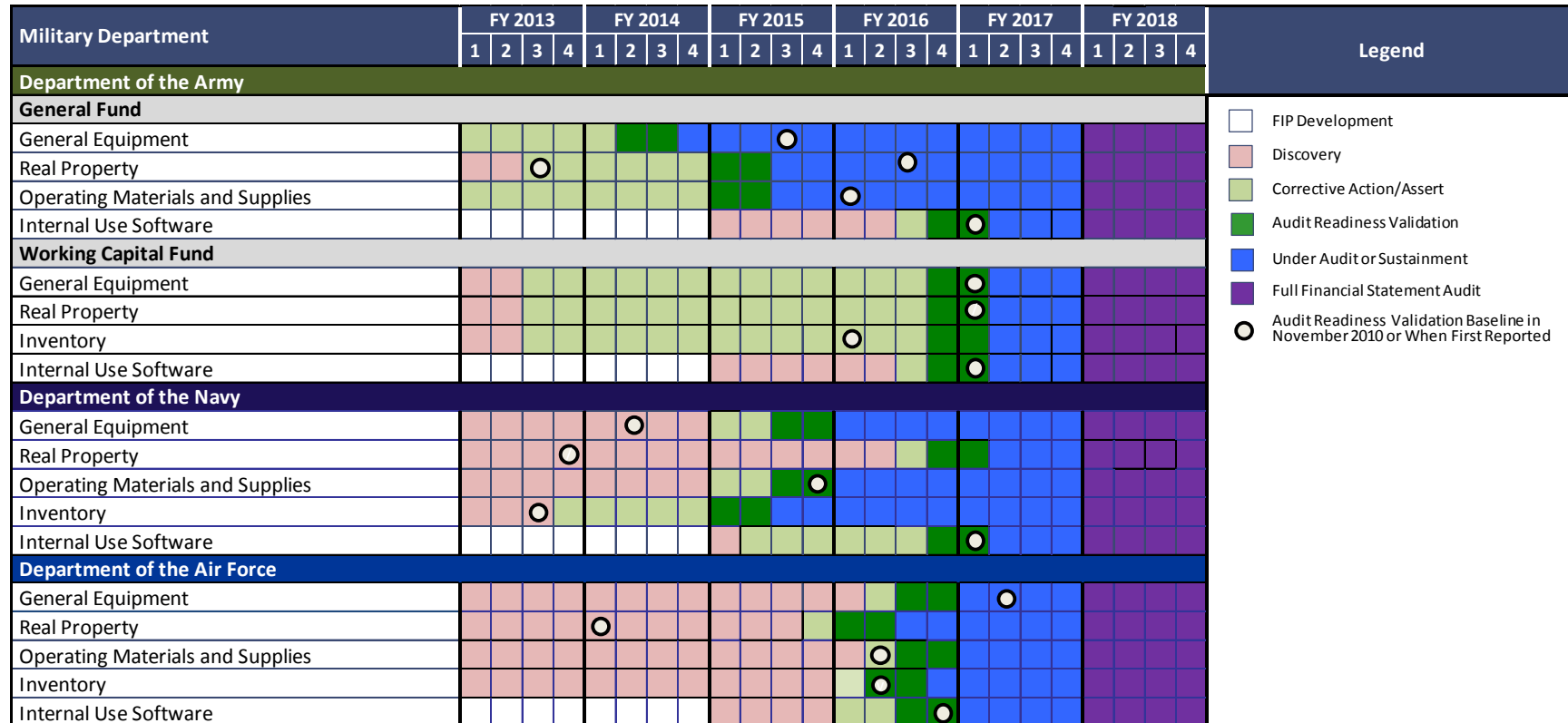
14-136

FIAR Plan Status Report

Figure II-3 provides a summary view of the Military Departments' plans for completing mission critical assets existence and

completeness audit readiness. As shown, all Components will assert audit readiness in FY 2016.

Figure II-3. Military Departments Mission Critical Assets Existence and Completeness Audit Readiness (Wave 3)

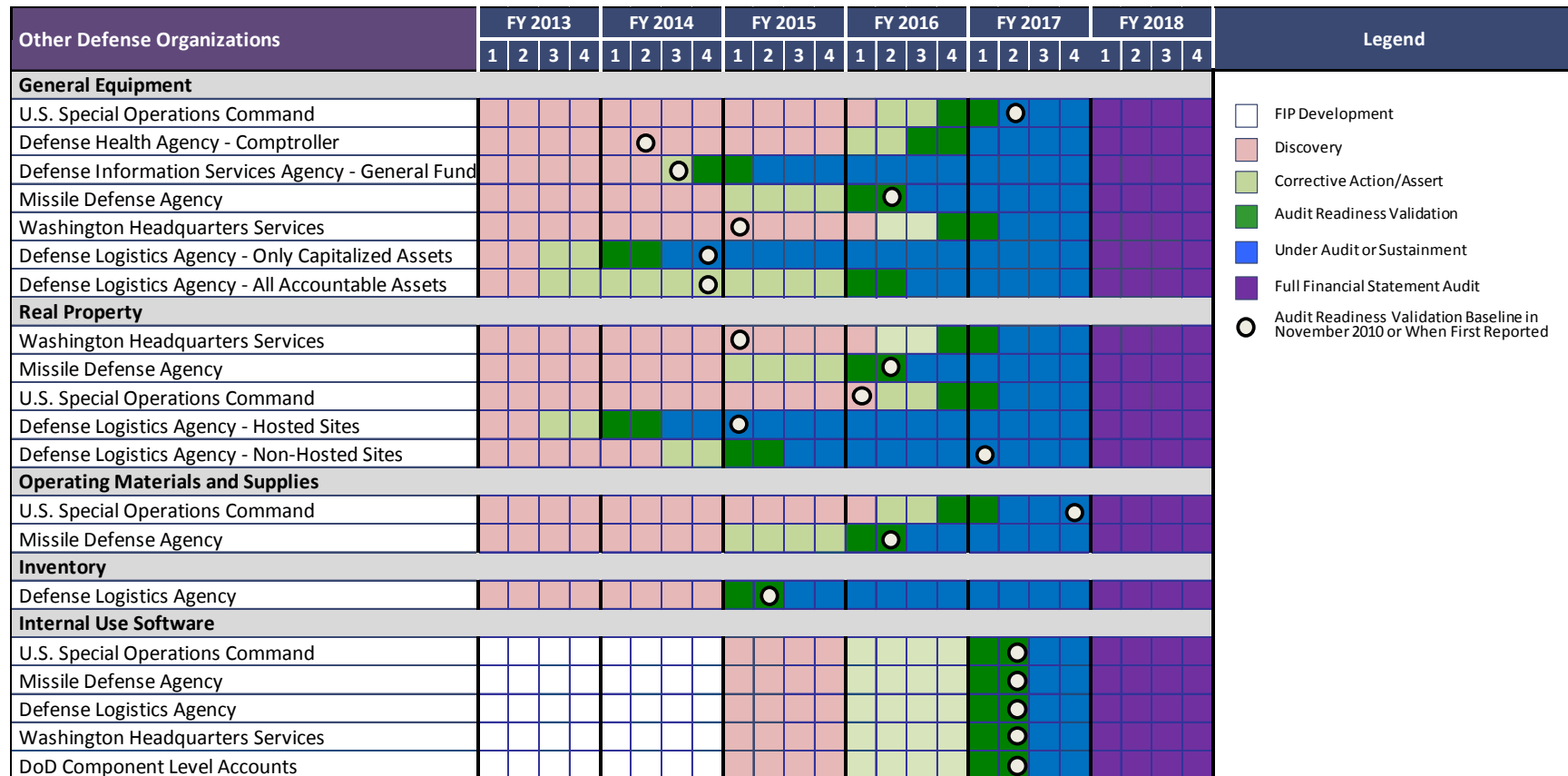


FIAR Plan Status Report

Figure II-4 provides the ODO status and plans for mission critical assets existence and completeness audit readiness. As shown in the figure, the ODOs will complete corrective actions and assert audit readiness in FY 2016. Because Internal Use Software was recently added as an assessable unit under mission critical assets existence

and completeness, only the Missile Defense Agency has completed developing milestones.

Figure II-4. Other Defense Organizations Mission Critical Assets Existence and Completeness Audit Readiness (Wave 3)



EXISTENCE AND COMPLETENESS AUDIT READINESS CHALLENGES

To complete mission critical asset existence and completeness audit readiness by June 30, 2016, the Department must overcome many DoD-wide challenges, including:

- The Department owns over \$168 billion of OM&S, which is 19 percent of DoD tangible assets reported on the Balance Sheet. OM&S comprises hundreds of thousands of different types of consumable items, some costing millions of dollars and some costing less than a dollar. Regardless of dollar value, all OM&S items must be recorded in management systems and pass existence and completeness tests. Examples of OM&S include spare and repair parts, ammunition, tactical missiles, aircraft configuration pods, and centrally managed aircraft engines held for consumption.
- The population of government-owned property furnished to contractors is incomplete and not consistently recorded in Component APSRs.
- System limitations impede reconciling the general ledger to transactional details amounts in APSRs. Manual processes are being developed to support audit readiness until systems with full capabilities can be deployed.
- Significant quantities of General Equipment stored by the Defense Logistics Agency (DLA) and managed as inventory in a DLA APSR, are owned by the Military Departments and must be reported on their Balance Sheets, requiring detailed data sharing and reconciliations.
- Ordnance assets owned by one entity and possessed by another complicate accurate reporting. For example, Army physically possesses 60 percent of all Air Force-owned munitions, as well as the munitions of the other Components. In this case, Air Force must work with the Army to gain assurance that internal controls governing Army-possessed and Air Force-owned munitions are effective.
- Real property assets acquired by a Military Department but used and controlled by an ODO must be reconciled and reported on the ODO's financial statements.
- Real property service provider roles and responsibilities need to be clearly defined and established in Memoranda of Understanding with the Military Departments to align assertion timelines and to ensure key controls and supporting documentation are designed properly and in place to support the customer assertions.

This Page Left Blank Intentionally

III. Full Financial Statements (Wave 4) by September 30, 2017

Wave 4 requires the Department to address many challenging financial reporting areas, such as Environmental and Disposal Liabilities and valuation of General PP&E, Inventory, and OM&S. In addition to the Statement of Budgetary Resources, the DoD financial statements comprise the General Fund Balance Sheet, Statement of Net Cost, Statement of Changes in Net Position, and the Working Capital Fund financial statements.

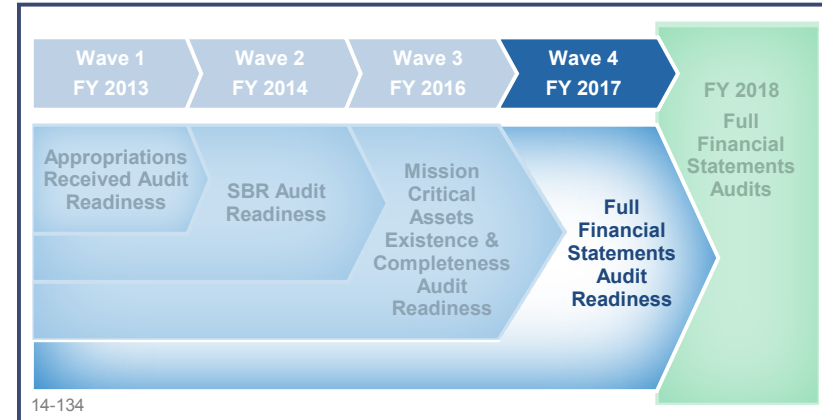
Audit readiness in Wave 4 builds on audit readiness progress in Waves 1, 2, and 3 (Figure III-1) and makes use of interdependencies between budgetary and proprietary accounting information, such as:

- Delivered Orders Unpaid, reported on the SBR, equate to a portion of Accounts Payable reported on the Balance Sheet
- Spending Authority from Offsetting Collections, reported on the SBR, includes amounts reported in Accounts Receivable – Intragovernmental on the Balance Sheet
- Unobligated Balances and Unpaid Obligations, reported on the SBR, correlate to Fund Balance with Treasury reported on the Balance Sheet
- Obligations incurred, reported on the SBR, equate to a substantial portion of Gross Costs reported on the Statement of Net Cost

PROGRESS TO DATE

The FIAR Strategy was designed to first achieve the FIAR priorities of audit readiness on the SBR and existence and completeness of mission critical assets before focusing on audit readiness of the full financial statements. Many of the financial improvements made under Waves 1, 2, and 3 contribute to achieving audit readiness on Wave 4.

Figure III-1. FIAR Strategy and Timeline



Examples of FIAR activity conducted during the other waves that support Wave 4 requirements include:

Army

- Improved Balance Sheet line items of Accounts Receivable and Accounts Payable by implementing corrective actions identified during IPA SBR examinations.
- Performed improvement activities on the Active Defense Environmental Restoration Program, a significant portion of Environmental Liabilities.
- Identified relationships between budgetary obligations incurred and the Statement of Net Cost using the General Fund Enterprise Business System (GFEBS).
- Worked with DFAS to develop an auditable Fund Balance with Treasury reconciliation process that includes internal controls to ensure reconciliation differences are resolved appropriately.

Navy

- Began establishing an effective information technology (IT) systems control environment by starting IT discovery efforts and

FIAR Plan Status Report

FISCAM assessments, and mitigating control deficiencies. This work included identifying the Department of the Navy (DON) target IT environment and system rationalization to reduce the number of systems across the DON.

- Began developing an asset valuation strategy based on the valuation guidance issued by the Office of the Under Secretary of Defense for Acquisition, Technology and Logistics (OUSD(AT&L)) that details the valuation methods and implementation timelines for each materially relevant asset category.

Air Force

- Completed valuation of aircraft, Intercontinental Ballistic Missiles, and satellites using a contract-based valuation methodology.
- Gathered asset valuation information during existence and completeness work at Air Force installations that will be used to value real property assets.
- Improved Accounts Payable by completing corrective actions resulting from the implementation of the SBR Automated

Reconciliation Tool.

- Completed an IPA examination of the Working Capital Fund (WCF) Civilian Pay processes and systems.
- Asserted audit readiness on Restoration of Environmental Liabilities.

Other Defense Organizations

The Defense Intelligence Agencies are on an accelerated audit schedule to meet a congressionally mandated deadline of achieving an unmodified audit opinion on their full financial statements by 2016. All Defense Intelligence Agencies have certified to the Director of National Intelligence and Congress that auditability is a priority and dedicated the resources necessary to achieve this objective.

The Intelligence Community Inspector General conducted a review of the Defense Intelligence Agencies' corrective action plans pending a full scope audit. The Defense Intelligence Agencies will undergo a full scope audit of their financial statements in 2014 by an IPA firm. Any identified weaknesses will be incorporated into corrective actions plans.

Figure III-2. Full Financial Statements Audit Readiness (Wave 4)

DoD Components	FY 2013				FY 2014				FY 2015				FY 2016				FY 2017				FY 2018				Legend
	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	1	2	3	4	
Army - Full Financial Statements (Wave 4)																									Corrective Actions/Assert
Navy - Full Financial Statements (Wave 4)																									Audit Readiness Validation
Air Force - Full Financial Statements (Wave 4)																									Full Financial Statements Audit
ODOs - Full Financial Statements (Wave 4)																									Audit Readiness Validation Baseline in November 2010 or When First Reported

Figure III-2 shows the planned timelines for Wave 4 for the Military Departments and the ODOs. As shown, the Components will complete corrective actions and assert audit readiness in FY 2017. During FY 2017, the Department will also complete preparations for the audits of DoD's full financial statements.

PLANNING FOR FULL FINANCIAL STATEMENTS AUDITS IN FY 2018

Lessons learned and experience from the SBA audits and existence and completeness of mission critical asset examinations will be considered as planning for audits of DoD's full financial statements begins. In November 2013, the FIAR Guidance was revised for Wave 4 requirements and included instructions for preparing Component work plans for achieving full audit readiness. Examples of changes to the FIAR Guidance include:

- Specific guidance for Working Capital Fund activities
- Property, Plant, and Equipment valuation guidance
- Inclusion of Cash and Other Monetary Assets, Investments, Other Assets, Environmental and Disposal Liabilities, and Other Liabilities
- Updated key capabilities, capability measures, and success criteria for Wave 4 assessable units

Working Capital Fund Statements

In addition to being required to produce audited General Fund statements, the Department is required to produce audited WCF financial statements. To date, minimal FIAR activity has taken place on the WCF statements for two reasons. First, the FIAR priorities were focused on the General Fund SBR and existence and completeness of mission critical assets. (WCF activities were included in the existence and completeness audit readiness of mission critical assets priority.) Second, WCF activity financial processes, controls, and systems are generally more reliable than the General Fund, because WCF activities operate like a business and

charge their customers in exchange for goods and services that cover costs and preclude a profit. Therefore, accuracy and reliability has been important.

Since WCF activities operate similar to commercial entities, accounting practices are primarily proprietary, accounting for revenue, expenses, and assets and liabilities on the Balance Sheet. As the WCF activities begin to develop financial improvement plans, the plans will be focused around lines of business or service, such as depot maintenance activities, supply activities, and transportation services.

WCF activities are subject to the same FIAR Methodology requirements as General Fund entities, including addressing the same risks of material misstatement and financial reporting objectives.

Balance Sheet

Early in the FIAR effort, the Department focused financial statement improvement efforts on the Balance Sheet. Although progress was very limited, past efforts resulted in useful experience, policy and financial management regulation changes, IT system changes, and involvement of functional communities, such as the OUSD(AT&L). That experience will assist the Department as it works on the Balance Sheet, using a similar line-item approach and engaging the same functional communities. Examples of Balance Sheet line items that will be assessable units in the Component financial improvement plans are:

- Fund Balance with Treasury
- Accounts Receivable
- General Property, Plant, and Equipment
- Operating Materials and Supplies
- Inventory
- Accounts Payable
- Environmental and Disposal Liabilities

Asset Valuation

To prepare for the extensive work to value DoD assets, the Department issued valuation policy and guidance including capitalization thresholds effective October 1, 2013. OUSD(AT&L) is overseeing the implementation of the policy changes and will be monitoring Component efforts to determine and document the value of most of General PP&E, OM&S, Inventory, and Environmental and Disposal Liabilities. The extensive work being performed in Wave 3 to document processes, test the effectiveness of controls, and ensure APSRs are complete supports the Department's effort to record and value its assets.

Other Statements and Footnotes

Wave 4 financial improvement activities will also address the preparation of the Statement of Net Cost and the Statement of Changes in Net Position. Although the Department has been annually preparing these statements, some work is required to ensure full audit readiness by September 30, 2017.

The Department must also ensure the footnotes to the financial statements are prepared in accordance with the reporting requirements and are audit ready by September 30, 2017. Footnotes provide important relevant information and more detail to the financial statement line items. For example, Footnote 10, General PP&E, Net, breaks down the Balance Sheet line of General PP&E into asset categories (e.g., Land, Leasehold Improvements, Software, and Buildings, Structures, and Facilities). Footnote 10 also provides the amounts of accumulated depreciation and amortization.

IV. Service Provider Audit Readiness

Service providers perform a variety of functions and services for the DoD Components, including:

- Accounting and Finance
- Civilian Personnel Management System Support
- Military and Civilian Pay
- Contract Management
- Real Property Construction
- Asset Acquisition, Storage, and Issuance
- Information Technology System Operations and Hosting Support

As a result, Component audit readiness often relies on service provider audit readiness. To support the Components' audit readiness efforts, service providers are working to achieve audit readiness and obtain reasonable assurance that their controls over operations and systems are designed and operating effectively. In addition, service provider systems must be interoperable and effectively functioning to provide Component systems with the information needed for accounting transactions and supporting documentation.

Upon completing financial improvement work, service providers undergo examinations conducted in accordance with the

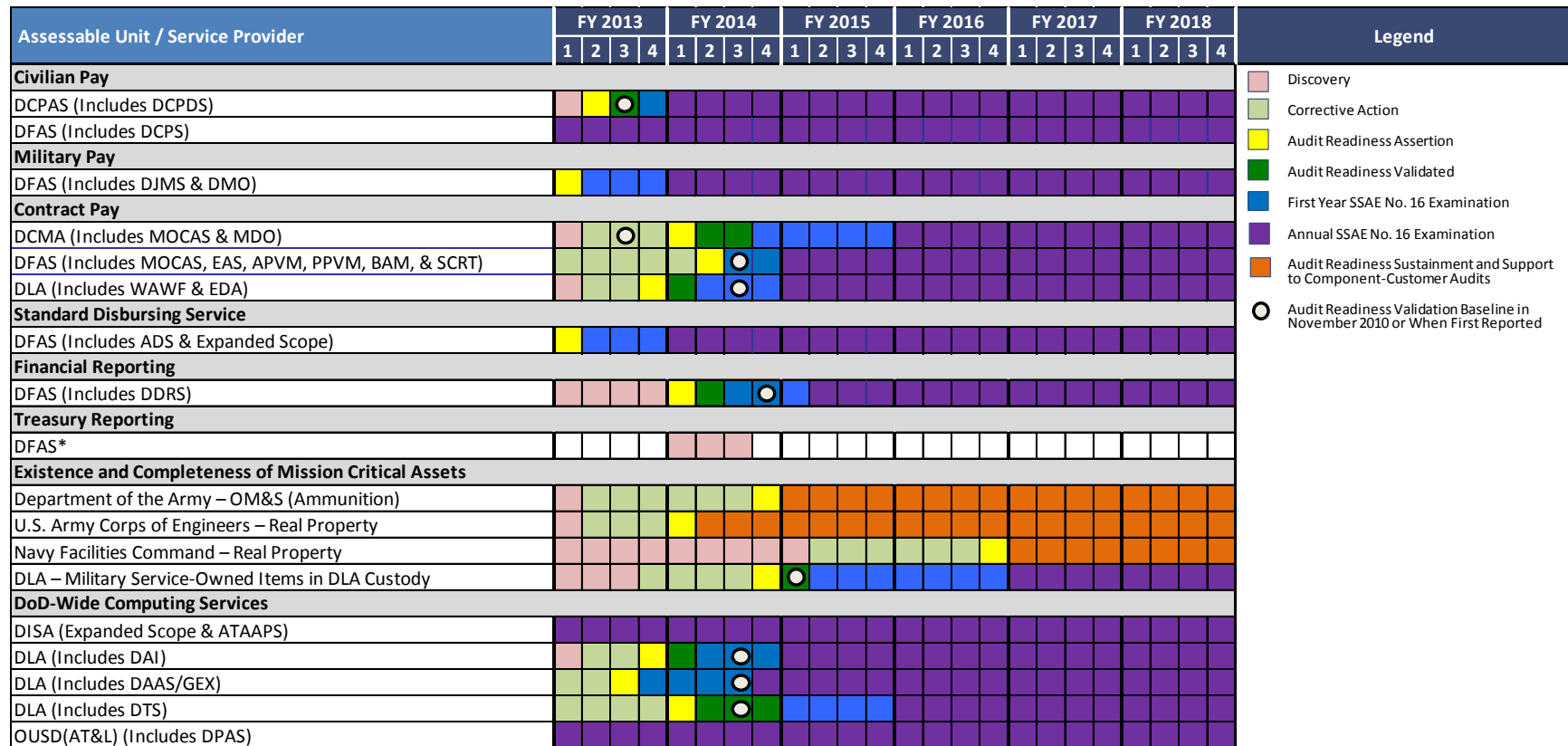
SSAE No. 16, Reporting on Controls at a Service Organization. To improve Department-wide efficiency, service providers with three or more Components as customers must obtain an SSAE No. 16 examination on controls. The results of the SSAE No. 16 examinations can then be relied on by a Component's financial statement auditors, saving time and money.

Service providers that are not required to produce an SSAE No. 16 examination must work with the Components to determine how they will support audit readiness efforts. Service providers are responsible for executing key tasks and activities in the Discovery and Corrective Action phases of the FIAR Methodology for the processes, controls, and systems that affect a Component's financial reporting objectives. Specifically, service providers must achieve financial reporting objectives by implementing control activities and providing supporting documentation that will ultimately be audited as part of a Component's financial statement audits. Coordinating service provider financial improvement activity is critical to audit readiness, therefore, service provider tasks and milestones are integrated into the Components' FIAR plans.

Figure IV-1 provides the service providers' status and plans for achieving audit readiness and conducting SSAE No. 16 examinations by assessable unit. As shown in the figure, the service providers will complete SBR audit readiness work in FY 2014, prior to the start of SBA audits in FY 2015. Also as shown, the service providers supporting mission critical assets existence and completeness audit readiness will complete financial improvement work in FY 2016 consistent with the Department's June 30, 2016, goal.

FIAR Plan Status Report

Figure IV-1. Service Provider Audit Readiness Plans



* DFAS is in the Discovery phase for Treasury Reporting and exploring opportunities to apply other SSAE No. 16 examinations.

V. Enterprise Resource Planning Systems

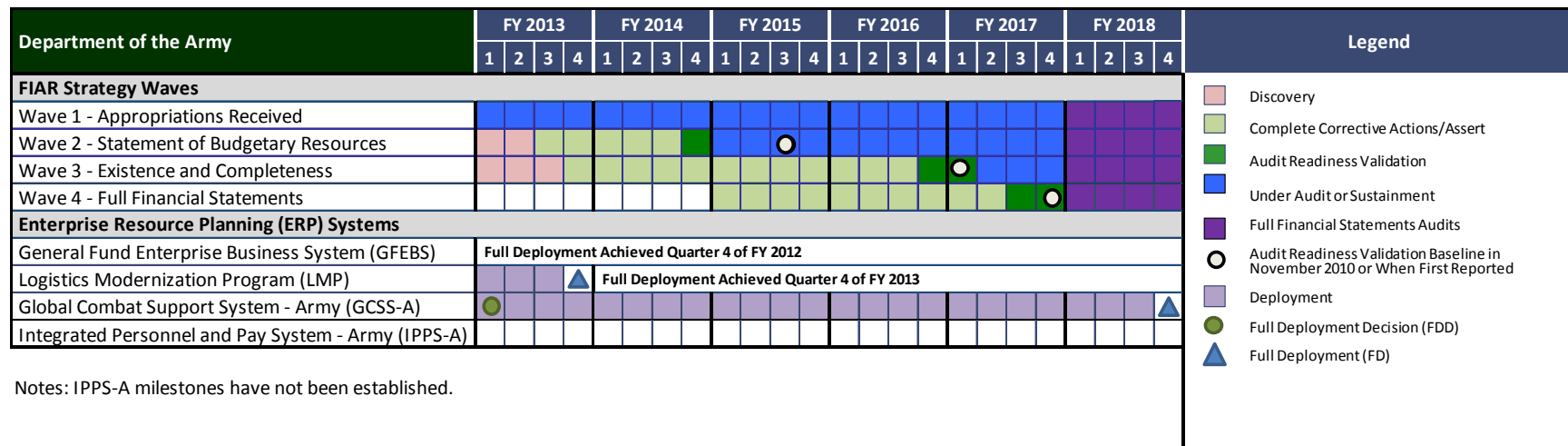
The Department's ability to produce auditable financial statements is, in part, dependent on establishing an audit-ready systems environment that includes Enterprise Resource Planning systems (ERPs). Automating internal, application, and interface controls; incorporating process and data standards; and ensuring correct posting logic and interoperability are essential. The Component plans for completing deployment of the ERPs vary, and some projected dates extend beyond the accelerated FY 2014 SBR audit readiness goal. As a result, the FY 2014 SBR audit readiness goals include a combination of ERPs and legacy business and financial systems.

DEPARTMENT OF THE ARMY

Figure V-1 shows the Army's audit readiness plans by wave as compared to its ERPs deployment schedule. The Army ERPs are:

- General Fund Enterprise Business System (GFEBS) is the General Fund web-enabled accounting, asset management, and financial system used to standardize, streamline, and share critical data across the active Army, Army National Guard, and Army Reserve.
- Logistics Modernization Program (LMP) is one of the world's largest, fully integrated supply chain, maintenance, repair and overhaul, planning, execution, and financial management systems. Its mission is to sustain, monitor, measure, and improve the modernized, national-level logistics support solution.
- Global Combat Support System – Army (GCSS-A) provides enterprise-wide visibility into various logistics areas and is a key enabler for the Army in achieving auditability.
- Integrated Personnel Pay System – Army (IPPS-A) is a hybrid solution using ERP software and agile development to deliver integrated personnel and pay capabilities.

Figure V-1. Army Audit Readiness and ERP Plans



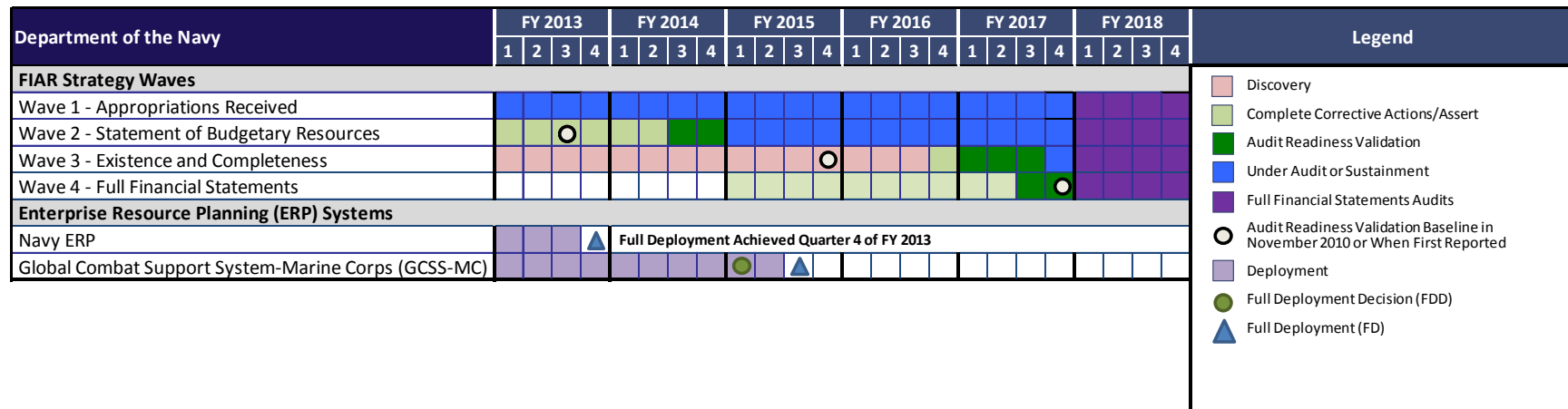
DEPARTMENT OF THE NAVY

Figure V-2 shows the DON's audit readiness plans by wave as compared to its ERPs deployment schedule.

The DON is deploying two ERPs:

- Navy ERP is the DON's financial system of record and streamlines the Navy's business operations, namely financial and supply chain management.
- Global Combat Support System – Marine Corps (GCSS-MC) provides the core of a modern, web-enabled, centrally managed, ERP software system to the Marine Corps.

Figure V-2. DON Audit Readiness and ERP Plans

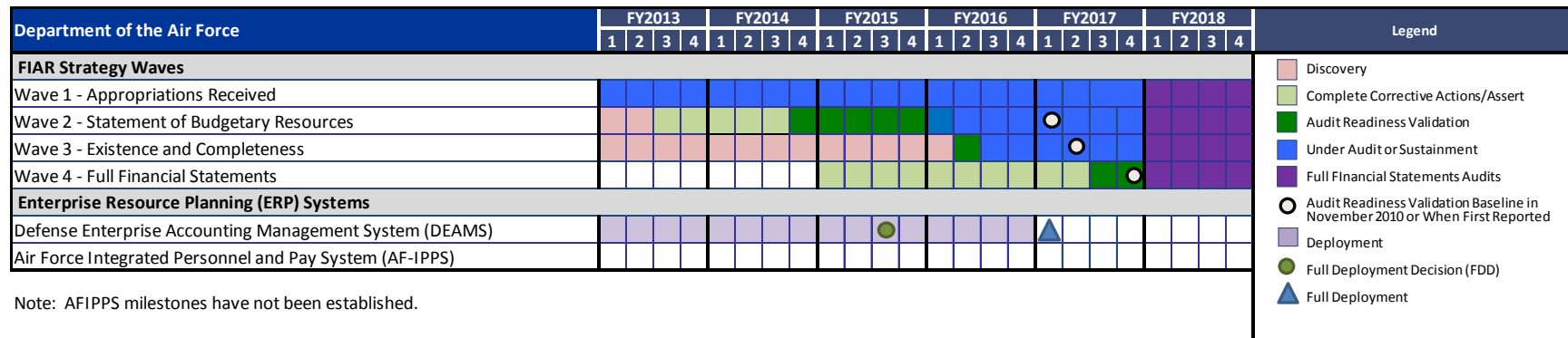


DEPARTMENT OF THE AIR FORCE

Figure V-3 shows the Air Force's audit readiness plans by wave as compared to its ERPs deployment schedule. The Air Force ERPs are:

- Defense Enterprise Accounting and Management System (DEAMS) is an automated accounting and financial management execution system for the Air Force and U.S. Transportation Command.
- Air Force Integrated Personnel and Pay System (AF-IPPS) is a comprehensive 24/7 self-service, web-based solution integrating personnel and pay processes into one system and maintaining an authoritative member record throughout the airman's career. An FFMIA-compliant system, AF-IPPS functionality will support audit readiness general and application controls; however, full deployment is not projected until Quarter 4 of FY 2018.

Figure V-3. Air Force Audit Readiness and ERP Plans



OTHER DEFENSE ORGANIZATIONS

The Defense Agencies Initiative (DAI) is modernizing the business environment at many of the Defense Agencies and other Defense organizations. The DAI objective is to achieve and sustain an auditable business environment with accurate, timely, authoritative financial data. The primary goal is to deploy a standardized system to improve cost of ownership, financial management capability, and achieve and maintain compliance with the Department's Business Enterprise Architecture and Standard Financial Information Structure.

To date, 12 Defense organizations have implemented DAI:

- Chemical Biological Defense Program (CBDP)
- Defense Applied Research Projects Agency (DARPA)
- Defense Health Agency (DHA)
- Defense Media Activity (DMA)
- Defense Prisoner of War/Missing Personnel Office (DPMO)
- Defense Security Service (DSS)
- Defense Technical Information Center (DTIC)
- Defense Technology Security Administration (DTSA)
- Defense Threat Reduction Agency (DTRA)
- Missile Defense Agency (MDA)

- Office of Economic Adjustment (OEA)
- Uniformed Services University of Health Sciences (USU)

An additional 10 Defense organizations will deploy DAI:

- FY 2015:
 - Defense Acquisition University (DAU)
 - Defense Contract Management Agency (DCMA)
 - Defense Micro Electronics Agency (DMEA)
 - DoD Educational Activity (DoDEA)
- FY 2016:
 - Defense Human Resources Activity (DHRA)
 - Defense Information Systems Agency (DISA) – General Fund only
 - Defense Security Cooperation Agency (DSCA)
 - DoD Office of the Inspector General (DoD OIG)
- FY 2017:
 - Defense Commissary Agency (DeCA)
 - Defense Contract Audit Agency (DCAA)

Appendix 1. Acronyms

Acronym	Definition
ADS	Automated Disbursing System
AF	Air Force
AF-IPPS	Air Force Integrated Personnel Pay System
APSR	Accountable Property System of Record
APVM	Accounting Pre-Validation Module
ATAAPS	Automated Time Attendance and Production System
AT&L	Acquisition Technology and Logistics
BAM	Business Activity Monitoring
CBDP	Chemical Biological Defense Program
CFO	Chief Financial Officer
CMO	Chief Management Officer
DAI	Defense Agencies Initiative
DAAS/GEX	Defense Automatic Addressing System/DoD Global Exchange
DARPA	Defense Advanced Research Projects Agency
DAU	Defense Acquisition University
DCAA	Defense Contract Audit Agency

Acronym	Definition
DCMA	Defense Contract Management Agency
DCPAS	Defense Civilian Personnel Advisory Service
DCPS	Defense Civilian Payroll System
DCPDS	Defense Civilian Personnel Data System
DDRS	Defense Departmental Reporting System
DDRS-AFS	Defense Departmental Reporting System – Audited Financial Statements
DEAMS	Defense Enterprise Accounting and Management System
DECA	Defense Commissary Agency
DFAS	Defense Finance and Accounting Service
DHA	Defense Health Agency
DHRA	Defense Human Resources Activity
DISA	Defense Information Systems Agency
DJMS	Defense Joint Military Pay System
DLA	Defense Logistics Agency
DMA	Defense Medical Activity

FIAR Plan Status Report

Acronym	Definition
DMEA	Defense Micro Electronics Agency
DMO	Defense Military Pay Office
DoD	Department of Defense
DoDEA	Department of Defense Educational Activity
DoD OIG	Department of Defense, Office of the Inspector General
DON	Department of the Navy
DPMO	Defense Prisoner of War/Missing Personnel Office
DPAS	Defense Property Accountability System
DPS	Defense Personal Property System
DRRT	Defense Reconciliation and Reporting Tool
DSCA	Defense Security Cooperation Agency
DSS	Defense Security Service
DTIC	Defense Technical Information Center
DTRA	Defense Threat Reduction Agency
DTS	Defense Travel System
DTSA	Defense Technology Security Administration
EAS	Entitlement Automation System

Acronym	Definition
EDA	Electronic Document Access
ERP	Enterprise Resource Planning System
ES	Executive Summary
FBWT	Fund Balance with Treasury
FD	Full Deployment
FDD	Full Deployment Decision
FFMIA	Federal Financial Management Improvement Act of 1996
FIAR	Financial Improvement and Audit Readiness
FIP	Financial Improvement Plan
FISCAM	Federal Information System Controls Audit Manual
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
GCSS-A	Global Combat Support System-Army
GCSS-MC	Global Combat Support System-Marine Corps
GF	General Fund
GFEBs	General Fund Enterprise Business System

FIAR Plan Status Report

Acronym	Definition
IPA	Independent Public Accountant (or Accounting Firm)
IPPS-A	Integrated Personnel Pay System – Army
IT	Information Technology
LMP	Logistics Modernization Program
MDA	Missile Defense Agency
MDO	Modifications Delivery Orders
MOCAS	Mechanization of Contract Administration Services
NDAA	National Defense Authorization Act
NFR	Notice of Findings and Recommendations
ODO	Other Defense Organization
OEА	Office of Economic Adjustment
OIG	Office of the Inspector General
OM&S	Operating Materials and Supplies
OUSD	Office of the Under 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)
PP&E	Property, Plant, and Equipment
PPVM	Payment Pre-Validation Module
SBA	Schedule of Budgetary Activity
SBR	Statement of Budgetary Resources
SCRT	Standard Contract Reconciliation Tool
SFIS	Standard Financial Information Structure
SSAE	Statement on Standards for Attestation Engagements
USTRANSCOM	U.S. Transportation Command
USU	Uniformed Services University of the Health Sciences
WAWF	Wide Area Workflow
WCF	Working Capital Fund
WHS	Washington Headquarters Services

This Page Left Blank Intentionally



FINANCIAL IMPROVEMENT AND AUDIT READINESS

KNOW YOUR BUSINESS

CONTROL YOUR FUTURE