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Dan McConnell
Ruotao Wang

Under the Supervision of Professor Howell Jackson
I. Introduction

The Chief Financial Officers Act of 1990 (CFO Act) represents an extraordinary moment in the history of financial management in the federal government. The role of financial managers has certainly progressed since the Constitution called for “a regular Statement and Account of the Receipts and Expenditures of all public Money.”

Although federal financial management was reformed over the years, the CFO Act represents a turning point whereby Congress not only increased the executive branch’s reporting requirements, but it also created a management structure aimed at fundamentally changing the role of financial managers in the federal government.

Focused on federal financial management, Section II of this paper will begin by describing the objective to bring more effective general and financial management practices to the federal government. Aimed at improving internal controls and the collection of relevant financial information, the section looks at how financial reporting has evolved and determines the extent to which it has delivered reliable financial reports. Since its passage, the CFO Act has been complemented by an assortment of legislation that together make up the current financial management environment, including laws such as the Government Management Reform Act of 1994 (GMRA) and the Accountability of Tax Dollars Act of 2002 (ATDA). Section III reviews financial management legislation in United States from the writing of the Constitution to the congressional hearings that ultimately led to the CFO Act, as well as the subsequent laws that have come to form the current body of federal financial management legislation.

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Section IV takes a more comprehensive look at the details of the CFO Act to understand the impact they have on various agencies affected by the law and the possible implications for financial management.

As federal agencies continue to improve their financial management systems and practices, many challenges continue to persist. In particular, the Department of Defense (DOD) has never received and unqualified audit opinion. Section V will discuss financial management within DOD, why DOD has failed to comply with the CFO Act after more than two decades, and its current plan to achieve auditability. The Government Accountability Office (GAO) reports “DOD financial management has been on GAO’s high-risk list since 1995 and, despite several reform initiatives, remains on the list today.” Consequently, Congress has increasingly taken an interest in DOD financial management in light of these “pervasive deficiencies in financial management processes, systems, and controls, and the resulting lack of data reliability.” DOD financial management covers a complex array of financial topics – including procurement, inventory, payroll, asset management, and real property – across a very complex organizational structure. In fact, its inability to achieve an unqualified audit has caused DOD’s accountability issues to extend beyond the agency by making an audit of the U.S. consolidated financial statements challenging, and as such DOD will likely continue to draw increased scrutiny from lawmakers.

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Finally, Section VI concludes by looking at the impact the CFO Act has had on federal financial management to date and discuss the prospects for DOD to succeed in meeting its various milestones.

II. Federal Financial Management

Financial managers have operated within the federal government since its earliest days and, as stewards of the taxpayers’ dollars, their efforts to ensure that each public dollar is spent wisely have remained a lasting goal for their successors. The role financial managers play has evolved throughout the years with the passing of several substantial pieces of legislation aimed at reforming how the government manages public funds. In the latter half of the 20\textsuperscript{th} Century, as technology improved and federal agencies became increasingly complex, the requirement to think more strategically about financial management became of increasing importance in Congress.\textsuperscript{8} In the chart below is an example of how legislation since the CFO Act has led to numerous reporting

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<th>Selected Federal Financial Reports: Authorities and Requirements</th>
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<td><strong>Report</strong></td>
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GMRA (1994)  
ATDA (2002) | Agency Head | Congress  
GAO  
OMB  
Treasury | 15-Nov |
President | 15-Dec |

requirements, all focused on financial management, and involving participation from both the legislative and executive branches.

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**Objectives of Federal Financial Reporting**

**Budgetary Integrity**

Federal financial reporting should provide information that helps the reader to determine:

- How budgetary resources have been obtained and used and whether their acquisition and use were in accordance with the legal authorization
- The status of budgetary resources
- How information on the use of budgetary resources relates to information on the costs of program operations

**Operating Performance**

Federal financial reporting should provide information that helps the reader to determine:

- Costs of providing specific activities and programs and the composition of and changes in these costs
- Efforts and accomplishments associated with federal programs and the changes over time and in relation to costs
- Efficiency and effectiveness of the government's management of its assets and liabilities

**Stewardship**

Federal financial reporting should aid in assessing the impact on the nation of the government's operations and investments and the implications for the future of the nation.

**Systems and Controls**

Federal financial reporting should assist report users in understanding whether financial management systems and internal accounting and administrative controls are adequate:

- Transactions are executed in accordance with budgetary and financial laws and other requirements, consistent with the purposes authorized, and recorded in accordance with federal accounting standards
- Assets are properly safeguarded to deter fraud, waste, and abuse
- Performance measurement information is adequately supported


III. Financial Management Legislation in the United States

When the CFO Act was passed in 1990, it became the foundation of a turning point for how the federal government performed financial management. OMB defines financial management as a structure to control and account for financial transactions and resources and to collect, analyze, and report data for financial decision-making. This section will explore the events leading up to this period as well as the effect they had on various government agencies’ efforts to improve their ability to execute efficient financial management capacity.

18th and 19th Century Financial Management Legislation

[T]here is a point...on which I should wish to keep my eye...a simplification of the form of accounts...so as to bring everything to a single centre[;] we might hope to see the finances of the Union as clear and intelligible as a merchant’s books, so that every member of Congress, and every man of any mind in the Union, should be able to comprehend them to investigate abuses, and consequently to control them.

- Thomas Jefferson, April 1802

Prior to the CFO Act, several governing provisions dominated financial matters in the federal government beginning with the Constitution’s establishment of the appropriations process. Article I, Section 9, paragraph 7 of the U.S. Constitution declares “No Money shall be drawn from the Treasury, but in Consequence of Appropriations made by Law; and a regular Statement and Account of the Receipts and Expenditures of

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all public Money shall be published from time to time.”\(^{10}\) This clause serves as the foundation for federal financial reporting, granting Congress the “power of the purse” as well as steady oversight by requiring a regular report of the receipts and expenditures of public money. Supreme Court Justice Joseph Story later remarked “a regular account of the receipts and expenditures is required to be published, that the people may know, what money is expended, for what purposes, and by what authority.”\(^{11}\)

In the following century, the Dockery Act expanded federal financial management in 1894 by providing “for a greater centralization of accounting functions and for a single audit of accounts in place of the ancient and cumbersome system of triplicate audits.”\(^{12}\) To accomplish this, it mandated that the Secretary of the Treasury provide Congress with “an accurate, combined statement of the receipts and expenditures during the last preceding fiscal year of all public moneys.”\(^{13}\)

**Budget and Accounting Act (BAA) of 1921**

For decades, however, coordination between the budgeting and accounting functions in the federal government failed to coalesce. The Budget and Accounting Act of 1921\(^ {14}\) was enacted in response to the agreement that a more centralized approach to financial management was needed and that participation would be required from both the executive and legislative branches. The 1921 act considered budgeting and accounting to be interdependent aspects of financial management, and in an attempt to link the two, began the practice of annual submissions of the President's budget to serve as the basis

\(^{10}\) U.S. Const. art. I, § 9, cl. 7.
\(^{13}\) The Dockery Act of 1894, 28 Stat. 205, 210 (1894).
for the governments accounting responsibility.\textsuperscript{15} However, despite such progressive reforms, budgeting and accounting never fully united and the two functions failed to fully integrate.

**Budget Accounting Procedures Act (BAPA) of 1950**

Another series of reforms began in 1950 when Congress passed the Budget Accounting and Procedures Act (BAPA) of 1950,\textsuperscript{16} making even more amendments to federal financial reporting requirements. BAPA authorized the Comptroller General, in consultation with OMB and Treasury, to “prescribe the principles, standards, and related requirements for accounting to be observed by each executive agency, including requirements for suitable integration between the accounting processes of each executive agency and the accounting of the Treasury Department.”\textsuperscript{17} Additionally, BAPA required agency heads to “establish and maintain systems of accounting and internal control.”\textsuperscript{18} BAPA further required the Secretary of the Treasury to use agencies’ financial information to prepare “such reports for the information of the President, the Congress, and the public as will present the results of the financial operations of the Government,”\textsuperscript{19} yet these reforms as well as those in the following decades failed to encourage the integration of budgeting and accounting.

\textsuperscript{15} Id.
\textsuperscript{16} Budget Accounting and Procedures Act, 64 Stat. 832, (1950).
\textsuperscript{17} 64 Stat. 835.
\textsuperscript{18} Id.
\textsuperscript{19} Id.
The Inspector General Act of 1978

The IG Act\textsuperscript{20} established independent inspector general offices in all agencies to conduct audits and investigations. In turn, the inspectors general recommend policies to promote economy, efficiency, and effectiveness. IG offices are further charged with detecting and preventing fraud, waste, and abuse as well as informing agency heads and Congress on any problems that arise.\textsuperscript{21}

The Federal Managers' Financial Integrity Act of 1982

The FMFIA requires executive agencies to maintain internal accounting and administrative controls in compliance with the standards prescribed by the comptroller general. According to the act, they must also evaluate their management accountability and control systems and report annually to Congress and the President with any plans necessary to resolve any deficiencies.\textsuperscript{22}

The Chief Financial Officers Act (CFO Act) of 1990

The CFO Act also gave the Office of Management and Budget (OMB) broad authority and responsibility for managing federal financial management, modernizing the government’s financial management systems in order to strengthen federal financial reporting. The act also created a new position in OMB, the Deputy Director for Management that became the federal government’s chief financial management official.

The CFO Act of 1990 was immediately followed the formation of the Federal Accounting Standards Advisory Board (FASAB) in October of that year. The FASAB’s objective was to define Generally Accepted Accounting Principles (GAAP) in an effort to

\textsuperscript{21} Id.
\textsuperscript{22} 31 U.S. Code § 3512 (1982).
ease the compilation of newly mandated federal financial reports,\textsuperscript{23} which would serve a fundamental role in accomplishing the CFO Act’s objectives.

**Government Performance and Results Act (GPMRA) of 1993**

Tied to the CFO Act are the Government Performance and Results Act of 1993, which was recently updated and enhanced by the Government Performance and Results Modernization Act of 2010. These Acts focus on government results, service quality, and customer satisfaction; integrate budget, financial, and performance measurement; and call for a strategic planning process, annual performance plans, and annual performance reports.

**Government Management Reform Act (GMRA) of 1994**

The GMRA set further guidelines for financial management, including the preparation of annual financial statements, streamlining management control, human resource management, and pay adjustments.\textsuperscript{24}

**Federal Financial Management Improvement Act (FFMIA) of 1996**

The FFMIA built upon the foundation of the CFO Act by emphasizing the need for agencies to have reliable mechanisms in place that could generate practical and timely information with which to make informed decisions and to maintain accountability. FFMIA requires inspectors general to report on whether the financial management systems in their agencies are compliant with federal requirements pertaining to accounting and the standard general ledger.\textsuperscript{25}


**Clinger-Cohen Act of 1996**

The Clinger-Cohen Act established a comprehensive approach for agencies to improve the acquisition and management of their information technologies by focusing information resource planning to support their strategic missions; applying capital planning and investment control processes linking budget formulation with execution; and restructuring the way they do their work before investing in information systems. The act also established Chief Information Officers (CIOs) at the agencies and entrusted them with financial systems responsibilities.

**Accountability of Tax Dollars Act (ATDA) of 2002**

The CFO Act was again expanded by the Accountability of Tax Dollars Act (ATDA) of 2002, which required federal agencies that lacked any existing requirement to prepare financial statements for audit to do so, making the requirement for audited financial statements essentially ubiquitous across government, as did the general concepts underlying the CFO Act.26

**Improper Payments Information Act (IPIA) of 2002**

The IPIA required agencies to monitor programs susceptible to improper payments and be capable of reporting such actions to Congress in an effort to reduce such payments.27

**Federal Funding Accountability and Transparency (FFATA) Act of 2006**28

The FFATA required OMB to establish a database of the recipients of federal grants, loans, and contracts, available publicly online.29

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29 See www.federalspending.gov
### Timeline of Financial Management Legislation

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<td>1802-67</td>
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<td>1984</td>
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<td>1993</td>
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<td>2010</td>
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<tr>
<td>2010</td>
<td>Government Performance and Results Modernization Act</td>
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IV. The Chief Financial Officers Act of 1990

The 1974 Congressional Budget and Impoundment Act created the Congressional Budget Office (CBO) as the legislative counterpart of OMB. In the face of rising deficits during the first term of the Reagan administration, Congress passed the Gramm-Rudman-Hollings Act, establishing deficit reduction goals and sequestration in an effort to balance the budget by 1991. Consequently, the time horizon was extended and fixed targets were abandoned in favor of adjustable ones.

The Single Audit Act of 1984 streamlined audits of federal assistance programs for state and local governments and OMB began issuing a series of circulars to provide central direction and guidance in financial management matters, such as internal control, prompt payment, and financial management systems.

Leading up to the CFO Act

As the desire for financial management reform gathered momentum within the federal government in the 1980s, Senator John Glenn’s “Federal Financial Management Reform Act of 1987,” quickly transformed into a Chief Financial Officer position for the whole federal government, eventually settling on a network of CFOs spread across the various executive agencies and led by a government-wide CFO. The U.S. General Accounting Office (GAO) was a moving force behind the CFO legislation. In 1987, the GAO drafted a comprehensive piece of legislation to reform financial management in the federal government. During hearings in the 100th Congress’ second session, GAO’s idea was hotly debated on issues such as where the CFO would reside and should the federal government transition to accrual accounting. Subsequently, various bills were introduced

30 S. 86, 100th Cong. (1988).

**Provisions of the CFO Act**

Described by the GAO as “the most comprehensive and far-reaching financial management improvement legislation since the Budget and Accounting Procedures Act of 1950,”32 the 1990 CFOs Act lays four cornerstones for Federal financial management reform including a strong leadership structure, long-range planning, strengthened accountability reporting, and audited agency-wide financial statements.33

The act is comprised of eleven, wide-ranging principal features that affected federal financial managers, auditors, and program managers at all levels of government.34

The figure below identifies the eleven features of the law followed by brief descriptions of each one.

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<td>11. Setting Accounting and Auditing Standard</td>
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33 CFO Act (1990).
34 Id.
1. OMB’s Leadership Role

The CFO Act provided for stronger centralized leadership by giving the Office of Management and Budget (OMB) broad, new authority and responsibility for directing federal financial management, modernizing the government’s financial management systems, and strengthening financial reporting. The act also creates a new position in OMB—the Deputy Director for Management, who is to be the government’s chief official responsible for financial management. Furthermore, the CFO Act also charges OMB’s Deputy Director for Management with overseeing many of the federal government’s general management functions including information policy, procurement policy, property management, and productivity improvement.35

2. Agency CFO’s

To provide a leadership structure linked to OMB’s financial management responsibilities at the department level, the CFO Act created chief financial officer36, as well as deputy chief financial officer, positions in 23 major agencies. Both are to have extensive financial management experience.

3. Consolidated Financial Management Operations

To consolidate responsibility for an agency’s financial management, the CFO Act requires that “an agency Chief Financial Officer shall oversee all financial management


36 Id.
activities relating to the programs and operations of the agency.”  

Under the act, an agency CFO’s responsibility will extend to every aspect of financial management related to operating agency programs.  

4. Enhanced Financial Management Systems

The CFO Act mandates that agency CFOs are to develop and maintain agency financial management systems that comply with:

- Applicable accounting principles, standards, and requirements;
- Internal control standards; and
- Requirements of OMB, the Department of the Treasury, and others.

Agency financial management systems are to provide complete, reliable, consistent, and timely information.  

5. Financial Management Plans

The CFO Act requires OMB to prepare and submit to the Congress a government-wide 5-year financial management plan. The plan, which is to be updated annually, is to describe planned OMB and agency activities for the next 5 fiscal years to improve the financial management of the federal government.  

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37 CFO Act at 10.
39 Id.
40 Id.
6. Financial Statements and Audits

The CFO Act requires that financial statements be prepared for trust and revolving fund operations and for agency programs that are substantially commercial functions.\(^{41}\)

<table>
<thead>
<tr>
<th>Original CFO Departments and Agencies</th>
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<tr>
<td>The Dept. of Agriculture</td>
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<td>The Dept. of Commerce</td>
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<td>The Dept. of Defense</td>
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<td>The Dept. of Interior</td>
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<td>The Dept. of Housing and Urban Development</td>
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<td>The Federal Emergency Management Agency</td>
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7. Annual Financial Management Status Reports

CFOs are responsible under the act for preparing annual reports containing a description and analysis of the status of agency financial management; and transmitting them to agency heads and OMB.\(^{42}\) OMB must also annually submit to the Congress a government-wide financial management report at the time of the President’s budget submission.\(^{43}\)

\(^{41}\) Id.
\(^{42}\) Id.
\(^{43}\) Id.
8. Financial Management Staffing

The act specifically places with the agency CFOs responsibility for recruiting, selecting, and training personnel to carry out agency financial management functions. Guidance for implementing the act states that agency CFOs should have authority to provide agency-wide policy advice on financial management staffing matters.44

9. The CFO Council

The CFO Act established the Chief Financial Officers Council. The act specifies that OMB’s Deputy Director for Management will chair the Council. Other members will be OMB’s Controller, Treasury’s Fiscal Assistant Secretary, and the agency CFOs appointed under the act. As specified in the act, the CFO Council’s functions are to advise agencies and coordinate their activities on financial management matters, such as:

1) Consolidating and modernizing financial systems
2) Improving the quality of financial data and information standards,
3) Strengthening internal controls
4) Developing legislation affecting financial operations and organizations45

10. Government Corporations

Government corporations are required to annually prepare a report on their internal accounting and administrative controls, consistent with the Federal Managers’ Financial Integrity Act requirement for reports by executive agencies.46 The CFO Act also requires the head of the corporation to submit an annual management report to the

44 Id.
45 Id.
46 Id.
President and the Congress no later than 180 days after the end of the corporation’s fiscal year and including information such as the corporation’s audited financial statements and report on internal controls.\textsuperscript{47}

11. Setting Accounting and Auditing Standards

The act called for agency financial systems to comply with applicable accounting principles, standards, and requirements. Also, audits of financial statements prepared under the act are to be done in accordance with generally accepted government auditing standards. The Budget and Accounting Procedures Act of 1950\textsuperscript{48} directs the Comptroller General, in consultation with OMB and Treasury, to prescribe accounting principles, standards, and related requirements for executive agencies to follow. The CFO Act provides that OMB’s Deputy Director for Management is to establish government-wide financial management policies and requirements for executive agencies. The Comptroller General, the Director of OMB, and the Secretary of the Treasury agreed to a cooperative approach to the standard-setting process by establishing the Federal Accounting Standards Advisory Board (FASAB).\textsuperscript{49}

Financial Management Progress and Concerns

Since the passage of the CFO Act of 1990, the federal financial community has made important strides in instilling strong accounting and financial reporting practices. This year, 23 of the 24 CFO Act agencies obtained an opinion from the independent

\begin{footnotesize}
\begin{itemize}
  \item \textsuperscript{47} Id.
  \item \textsuperscript{48} 31 U.S.C. § 3511 (a).
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\end{footnotesize}
auditors on their financial statements. Out of the 24 major “CFO Act agencies,” there were 22 clean opinions, one qualified opinion, and only one remaining disclaimer in FY 2013.\textsuperscript{50} In addition, 29 auditor-identified material weaknesses were reported in FY 2013, an approximate 52 percent decline from the 61 material weaknesses that were identified at the start of this past decade.\textsuperscript{51} An increasing number of federal agencies have initiated and sustained disciplined and consistent financial reporting operations and implemented effective internal controls around financial reporting.

These efforts have resulted in improved results on financial statement audits. However, weaknesses in basic financial management practices and other limitations continue to prevent one major agency, and the Government as a whole, from achieving an audit opinion.


\textsuperscript{51} Id.
V. Financial Management in the Department of Defense

Implementation of the CFO Act of 1990 in DOD

The Department of Defense initially embraced the CFO Act as a valuable opportunity to improve financial management within the department. Initiatives were initiated in response to the Department's Defense Management Report (DMR), approved by President Bush in July 1989 prior to passage of the Act. The DMR highlighted the need to improve the management infrastructure within DOD and, in particular, its financial management procedures. With proposals such as the joint Defense Finance and Accounting Service (DFAS) in place, the Department concluded that reforms already in underway would fulfill the provisions of the new CFO Act. Specifically, it stated that a DOD “review of the Comptroller/CFO's current responsibilities shows that DOD is well equipped to respond to the requirements of the new CFO legislation without changes to the organizational alignments within the Department” In fact, the example of DFAS’s role in consolidating DOD’s finance and accounting operations early in DOD’s implementation of the CFO Act’s requirements reveals a potential source of DOD’s early optimism. DFAS is responsible for executing statutory and regulatory financial reporting requirements and preparing consolidated financial statements required by the CFO Act. Since its inception, the agency has consolidated more than 300 installation-level offices into nine DFAS sites and reduced the number of systems in use from 330 to 111. DFAS has steadily reduced operating costs and has returned those savings to its customers in the

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form of decreased bills and improved service. These savings are a result of the agency's robust search for continuous innovation and enhanced business practices. DFAS remains the world's largest finance and accounting operation.\textsuperscript{55}

**Resource Constraints in DOD**

Despite early optimism, DOD is one of the most complex departments in the federal government. Unclear to officials at the time, DOD’s complexity would prove to be a significant contributing factor to its inability to fully comply with the CFO Act.

Due to the fact that DOD repeatedly failed to produce a financial report capable of being audited, Congress limited DOD’s ability to conduct annual financial statement audits under Section 1008 of the FY 2002 NDAA.\textsuperscript{56} To understand exactly what impact this will have on DOD as they increasingly are required to conduct more annual audits, the internal capacity within DOD can be measured in terms of annual budget appropriations. The primary organizations within DOD that conduct financial audits and financial management are the Defense Contract Audit Agency (DCAA), the Defense Contract Management Agency (DCMA), and the Inspector General (IG). When analyzing these three organization’s annual appropriations over the previous decade, it is revealed that there has been very little growth in resources dedicated to these organizations.

\textsuperscript{55} *Id.*
\textsuperscript{56} National Defense Authorization Act § 1008.
From the chart above, it becomes apparent that the organization that experiences the largest share of budget growth is also the organization least directly involved in financial auditing, rather the DCMA is predominately involved in contract management.

**DOD’s Size and Complexity**

Audited financial statements were the key aspect of the CFO Act that DOD sought to include early in its financial management improvement program. Although initial planning seemed as if DOD could quickly and efficiently implement the legislation, DOD continuously failed to make progress toward producing audited financial reports. From 1994 to 2005, DOD began a number of audit efforts with limited success. The Defense Department was not the only agency struggling—even much smaller agencies were taking as long as 5 to 7 years to achieve an opinion. Meanwhile, DOD’s size, complexity, and geographic dispersion were growing as the nation entered the global war on terrorism.\(^5^7\)

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In 2012 DOD reported $769 billion in net costs and over $2 trillion dollars in assets.\textsuperscript{58} In addition to the three Military Departments of the Army, Navy, and Air Force, all very large organizations in their own right, DOD also includes eight Combatant Commands, 17 Defense Agencies, ten Field Activities, six Joint Service schools, the Joint Chiefs of Staff, the Inspector General, and many other organizations, such as the National Guard Bureau. It manages almost three million employees and provides benefits to another two million retirees and their family members. Adding to the complexity, more than 450,000 employees are overseas, both afloat and ashore.\textsuperscript{59}

The Department’s physical infrastructure consists of several hundred thousand buildings and structures located at more than 5,000 locations, worldwide. When added together, DOD uses over 30 million acres of land, ranging from unoccupied sites supporting a single navigational aid that sit on less than one-half acre, to the Army's vast White Sands Missile Range in New Mexico with over 3.6 million acres and the Navy’s large complex of installations at Norfolk, Virginia that includes 78,000 employees. Thus, comparing DOD to another federal agency or a large multi-national corporation does not fully reflect its size.\textsuperscript{60} Although auditability was arguably now even more important, it often fell in priority as focus intensified on national security and the urgent needs of the warfighter.

\textsuperscript{58} Id.  
\textsuperscript{59} Id.  
\textsuperscript{60} Id.
**DOD’s Financial Improvement and Audit Readiness Plan**

The Financial Improvement and Audit Readiness (FIAR) Goal is to improve the Department’s financial management operations while maintaining support those serving in the military and stewardship of taxpayer dollars.\(^\text{61}\)

Each of the DOD’s financial statement line items is affected by the unique and complex accounting and auditing challenges described above. DOD’s strategy assembles and prioritizes each business process, subject to reporting on various financial statement line items, within four waves and summarizes the steps necessary to address each wave. The waves and steps are prioritized based on the OUSD(C) priorities, known challenges, and the related dependencies of financial statements, line items and business processes on one another.\(^\text{62}\) Waves representing significant levels of effort and accomplishments are noted below.


DOD’s Strategy provides coverage of all financial statements, while prioritizing and improving information most often used by DOD. Furthermore, as depicted in the Figure above, the four waves will lead to interim audit-ready milestones and ultimately to a full audit readiness.

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\(^{62}\) Id. at 9.
Wave 1 – Appropriations Received Audit

A precise accounting of DOD’s budget activity, such as appropriations, is needed to appropriately commit, obligate, and expend funds. Securing this information in a timely and accurate fashion will ensure that DOD has the ability accomplish its mission while avoiding over-obligation due inaccurate budget information, resulting in Anti-deficiency Act violations. Successfully achieving audit-readiness of Wave 1 processes will demonstrate to Congress DOD’s appropriations are accurately accounted for, verified in its financial reports, bolstering Congress’s confidence in future DOD budget requests.63

Wave 2 – SBR Audit

A successful SBR audit presents all budgetary resources that a reporting entity has available, the status of those resources at period end, a reconciliation of changes in obligated balances from the beginning to the end of the period, and cash collections and disbursements for the period reported, for example, the reconciliation and traceability of interagency agreements, including Military Interdepartmental Purchase Requests (MIPR).64

Wave 3 – Mission Critical Asset Existence & Completeness (E&C) Audit

A reporting entity’s successful Mission Critical Asset E&C Audit will ensure that all its assets on record exist (Existence), and all of the it’s assets are recorded appropriately in it’s system (Completeness). A successful reporting entity must design

63 Id.
64 Id. at 10.
and implement physical inventory count procedures and documentation that will withstand audit scrutiny.\textsuperscript{65}

**Wave 4 – Full Financial Statement Audit**

Requirements for this wave include audit-readiness of all inventory, account balances, and financial transactions impacting the Balance Sheet, Statement of Net Cost, and Statement of Changes in Net Position not covered by Waves 2 or 3 pertaining to the reporting entity. FIAR priorities require devoting resources and efforts toward completing Waves 1 through 3 before beginning work on Wave 4. Nevertheless, much of the work required to complete Waves 1 through 3 impacts the requirements for Wave 4.

In a DOD memo dated October 13, 2011, Secretary of Defense Leon Panetta emphasized the importance of the department’s efforts thus far and directed DOD to focus on key elements of the FIAR Plan in an effort to meet the legal requirements to achieve full audit readiness for all DOD financial statements by 2017.\textsuperscript{66} Furthermore, its May 2013 FIAR Plan Status Report reiterated the DOD’s commitment to achieving its audit readiness goals, but noted that absent a stable budget environment, DOD efforts were subject to increased risk.\textsuperscript{67}

\textsuperscript{65} Id. at 12.
\textsuperscript{67} In accordance with the National Defense Authorization Act for fiscal year 2010, the DOD Comptroller provides reports to relevant congressional committees on the status of DOD’s implementation of the FIAR Plan twice a year—no later than May 15 and November 15, which includes risk assessments.
VI. Conclusion

Since the passage of the CFO Act of 1990, the federal financial community has made important strides in instilling strong accounting and financial reporting practices within federal government. During FY 2013, 23 of the 24 “CFO Act” agencies obtained an opinion from independent auditors on their financial statements and of the 24 major “CFO Act” agencies, there were 22 unqualified opinions, one qualified opinion, and only one remaining disclaimer in FY 2013. Additionally, the fraction of auditor-identified material weaknesses reported in FY 2013 constituted a 52 percent decline from those identified at outset of last decade. It is a positive sign that an increasing number of federal departments and agencies are sustaining disciplined and consistent financial reporting operations.\(^6\)

Despite the many benefits that have been derived from the CFO Act, DOD’s disclaimer of opinion\(^6\) on its consolidated financial statements mentioned in the previous paragraph underscores the potential challenges to the federal government’s ability to improve its financial management overall. DOD has a significant impact on the rest of the federal government’s financial condition; in fact, DOD represented roughly 33 percent of the federal government’s reported total assets as of September 30, 2013. Furthermore, approximately 16 percent of the federal government’s reported net cost for fiscal year 2013 relate to the Department of Defense.\(^7\)

On October 13, 2011, the Secretary of Defense directed DOD to achieve audit readiness goals focused on interim milestones by the end of 2014\textsuperscript{71} in an effort to meet the mandate passed by Congress in the FY 2010 National Defense Authorization Act (NDAA) to achieve full audit readiness across DOD’s complete set of financial statements by the end of 2017.\textsuperscript{72} In light of these targets, there are a number of roadblocks to be aware of as 2017 approaches. Should one of the challenges described below appear, it could indicate further delays for DOD in its pursuit to audit its complete set of financial statements.

1. \textbf{Budgetary Turmoil Effect on Audit Readiness}\textsuperscript{73}

In recent years, budgetary turmoil has impeded audit readiness progress. By budgetary turmoil, the Department is referring to:

- A government shutdown requiring furloughs across the DOD civilian workforce
- Multiple threats of government shutdown, disrupting FIAR activity and plans
- Long-term continuing resolutions requiring unexpected and time-consuming management action
- A substantial period under sequestration (approximately 6 months), additionally resulting in significant civilian furloughs

Budgetary challenges severely affect senior leadership’s resources, the civilian workforce, and availability of funds.


2. Availability of Individual Auditors\textsuperscript{74}

- It is likely that large numbers of auditors will be required to conduct DOD-wide audits given its tremendous size and complexity.
- Moreover, DOD operates numerous information systems that will require proficiency on the part of the auditors across the various systems.
- Because of DOD’s size and its current relationships with a large number of public accounting firms that independence issues could further complicate the availability of the necessary auditors. Firms that have already been working with components of DOD may be precluded from a DOD-wide audit.

3. Capacity of DOD’s Inspector General\textsuperscript{75}

According to the CFO Act, DOD’s Inspector General (IG) is responsible for auditing DOD’s financial statements. Because the DOD IG has limited its annual financial statement audits in accordance with Section 1008 of the FY 2002 NDAA,\textsuperscript{76} the possibility exists that DOD’s IG has neither the requisite numbers of experienced auditors nor the requisite funding to prepare adequately for audits in FY 2015.

\textsuperscript{74} Id.

\textsuperscript{75} Id.

\textsuperscript{76} National Defense Authorization Act § 1008.