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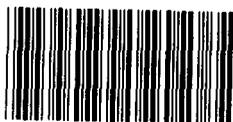
United States General Accounting Office

GAO

Transition Series

December 1992

National Security  
Issues



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GAO/OCG-93-9TR

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1. The first part of the document discusses the importance of maintaining accurate records of all transactions. It emphasizes that proper record-keeping is essential for the integrity of the financial system and for the ability to detect and prevent fraud. The document also notes that records should be kept for a sufficient period of time to allow for a thorough review if necessary.

2. The second part of the document outlines the specific requirements for record-keeping. It states that all transactions must be recorded in a clear and concise manner, and that the records must be accessible to authorized personnel at all times. The document also requires that records be kept in a secure and confidential manner, and that they be protected from unauthorized access or disclosure.

3. The third part of the document discusses the role of internal controls in ensuring the accuracy and reliability of the financial records. It notes that internal controls should be designed to prevent errors and to detect any irregularities in the financial data. The document also emphasizes that internal controls should be regularly reviewed and updated to reflect changes in the business environment.

4. The fourth part of the document addresses the issue of data security. It states that all financial data must be protected from unauthorized access, use, or disclosure. The document also requires that appropriate security measures be implemented to protect the data, and that these measures be regularly tested and updated.

5. The fifth part of the document discusses the importance of training and education for all personnel involved in the financial system. It notes that personnel should be trained in the proper use of the financial system and in the importance of maintaining accurate records. The document also requires that personnel be kept up-to-date on any changes in the financial system or in the requirements for record-keeping.

6. The sixth part of the document discusses the role of external audits in ensuring the accuracy and reliability of the financial records. It notes that external audits should be conducted regularly and that the results of these audits should be used to identify and correct any weaknesses in the financial system. The document also emphasizes that external audits should be conducted in a transparent and objective manner.

7. The seventh part of the document discusses the importance of communication and collaboration between all stakeholders in the financial system. It notes that clear communication is essential for ensuring that all personnel understand their roles and responsibilities and for identifying and resolving any issues that may arise. The document also requires that all stakeholders be kept up-to-date on any changes in the financial system or in the requirements for record-keeping.

8. The eighth part of the document discusses the importance of monitoring and reporting on the performance of the financial system. It notes that regular monitoring and reporting are essential for identifying and addressing any issues that may arise. The document also requires that appropriate metrics be used to measure the performance of the financial system and that these metrics be reported to the appropriate authorities.

9. The ninth part of the document discusses the importance of maintaining the integrity of the financial system. It notes that the financial system should be designed to prevent any unauthorized access or modification of the data. The document also requires that appropriate security measures be implemented to protect the data and that these measures be regularly tested and updated.

10. The tenth part of the document discusses the importance of maintaining the confidentiality of the financial system. It notes that all financial data must be protected from unauthorized access, use, or disclosure. The document also requires that appropriate security measures be implemented to protect the data and that these measures be regularly tested and updated.



United States  
General Accounting Office  
Washington, D.C. 20548

Comptroller General  
of the United States

December 1992

The Speaker of the House of Representatives  
The Majority Leader of the Senate

In response to your request, this transition series report discusses major defense policy, management, and program issues facing the Congress and the new administration. These issues involve (1) reassessing military roles and missions; (2) managing the downsized and restructured force; (3) reassessing U.S. commitments, forward presence, and security assistance programs; (4) controlling the spread of weapons of mass destruction; (5) reforming weapons system acquisition while preserving the industrial base; (6) addressing environmental challenges; (7) following through on inventory and other management initiatives; and (8) improving financial management.

As part of our high-risk series on program areas vulnerable to waste, fraud, abuse, and mismanagement, we are issuing related reports; Defense Weapons System Acquisition (GAO/HR-93-7, Dec. 1992); Defense Inventory Management (GAO/HR-93-12, Dec. 1992); and Defense Contract Pricing (GAO/HR-93-8, Dec. 1992).

The key GAO products upon which this transition series report is based are listed at the end of the report.

We are also sending copies of this report to the President-elect, the Republican leadership of the Congress, the appropriate congressional committees, and the Secretary-designate of Defense.

Charles A. Bowsher

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# National Security Issues

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At the time of our 1988 transition series, the defense budget had started to decline from its peak in the mid-1980s, and relations with the Soviet Union were allowing the United States to look for ways to further reduce defense spending. There was no hint, however, of the momentous changes that were about to take place. In 1989, the Berlin Wall fell, and the Warsaw Pact crumbled as a military force. In 1990, Iraq invaded Kuwait and triggered Operations Desert Shield and Desert Storm. In 1991, an attempted military coup in the Soviet Union failed and hastened the dissolution of the country into 15 separate republics. There was general agreement that the Cold War was over.

In response to these events, the Department of Defense (DOD) has begun to cut its forces and is now moving toward a 25-percent reduction by 1997. DOD is halfway toward reducing military and civilian forces by 800,000. It is proposing to pull about half of its forces out of Europe and is closing many bases around the world and at home. Even with these cuts, the defense budget is still targeted at over \$275 billion in fiscal year 1997. Many in the Congress argue that these cuts are not enough, that they do not fully reflect the dramatic changes that have taken place in the world, and that they will result

in a force that is just a smaller version of the Cold War force. The major issues cited in this transition series report revolve around this debate. How much can the United States reduce its force? How much can be saved? What shape should the new force have?

Reducing defense spending will be complicated by a number of financial issues that are currently not fully recognized in DOD's spending plans. There is a significant mismatch between the \$1.4 trillion fiscal year 1993-97 defense spending plan and budget realities. The spending plan does not recognize (1) over \$35 billion in potential weapons cost growth, (2) about \$12 billion in congressional actions delaying some proposed program terminations, (3) an estimated \$5.4 billion in funding for defense conversion to commercial activities, and (4) \$60 billion in additional cuts proposed by the President-elect. In addition, the spending plan assumes \$53 billion in management savings, the majority of which may not be achieved, and \$5 billion in base closure savings that will not be realized during the period. As a result, DOD may be faced with additional program reductions of over \$150 billion.

Additional items will add pressure for more defense spending in the longer term. For example, cleaning up hazardous waste on defense property is now estimated at a total of \$24.5 billion, and disposing of chemical weapons will cost at least \$8 billion. Both these estimates are expected to grow.

In addition to these new issues, we also cite some of the same issues that were present in 1988. At that time, we highlighted inventory management and weapons acquisition as two areas needing focused management attention. The Department has taken major steps over the past 4 years to tackle the numerous problems we cited, and if properly implemented, these initiatives will go a long way toward improving the efficiency and effectiveness of these activities. Because of the resources consumed by these functions and their importance to maintaining defense forces, we continue to highlight them this year and urge that the Congress and the new administration go even further in making fundamental reforms.

In 1988, we also pointed out efficiencies that are possible through a careful examination of military service roles and missions. Little was done to address that issue, and this same concern was expressed by the

Congress last year when it called on DOD to do such an analysis. We again believe that this analysis will be crucial to streamlining our military forces for the post-Cold War era. We also cautioned in 1988 of the dangers of recreating the "hollow force" that existed in the post-Vietnam era by cutting readiness and training too deeply and too fast. Performance in the Persian Gulf War indicated that readiness was at very high levels, but as deep cuts in the budget are proposed, the same danger exists during the 1990s.

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# Reassessing Military Roles and Missions

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The end of the Cold War has materially altered the international security environment—setting the stage for the most fundamental and potentially far-ranging reexamination of the nation's defense policy and structure in 40 years. Instead of the global threat from the Soviet Union, the United States now faces potential regional threats around the world, many of which cannot be fully anticipated. Policymakers are confronted with complex and difficult choices as they attempt to achieve a critical balance between the need to protect national security interests and the affordability of programs to that end. The complexity and difficulty of the choices will be compounded by the huge federal budget deficit and emerging but unpredictable threats to U.S. interests.

The Congress has directed the Joint Chiefs of Staff to examine the roles and missions of the armed services to eliminate unnecessary redundancy and duplication. Making changes will require taking on entrenched bureaucracies in the Pentagon and power centers in the military services, as well as prevailing cultural attitudes—both internal and external to the defense establishment. Our work has shown, for example, that individual services have developed and

acquired weapons systems to meet particular missions without adequate consideration of other services' capabilities. Close air support systems and antiarmor systems developed by the Air Force, the Army, and the Marines are two examples.

A reexamination of military roles and missions appears to offer many opportunities to provide a more cost-effective means of meeting defense needs that exist today. In the area of conventional warfare, for example, DOD should consider whether the current number of Army light infantry and Marine divisions is more than what is necessary to meet expected threats. Opportunities also exist for placing less reliance on carrier battle groups by changing the way they have been historically deployed. Increasing the use of alternative naval forces, such as surface action groups and amphibious ready groups, may reduce the demand for the much more expensive carrier battle group.

Scrutiny also needs to be given to strategic roles and missions. Our recent analysis of the performance of the strategic nuclear triad's weapon systems should help policymakers weigh options and costs and make critical choices about future

requirements for deterrence. We found that sea-based strategic weapons are more cost-effective and less vulnerable than the other two strategic legs. We also found that the B-2 is extremely costly, at over \$2 billion apiece, and of questionable value as a strategic bomber. The B-1B and the B-52 will continue to remain a viable strategic bomber force for years to come.

In the post-Cold War era, the military services will be challenged to perform new and enhanced missions in such areas as peacekeeping, narcotics interdiction, and disaster relief. United Nations' requests for DOD assistance—including supplies, military airlifts and sealifts, logistics, and personnel—for peacekeeping operations have increased substantially in the past 2 years and may likely continue in the near future. Similarly, DOD's involvement in narcotics control and the agency's assistance in drug interdiction efforts have expanded considerably: DOD's contribution rose from \$300 million in fiscal year 1989 to \$1.2 billion this year. DOD has also increased its involvement in providing humanitarian and disaster assistance in such places as Somalia and Bangladesh as well as within the United States. The value of these missions, as well as the resources devoted to them, must be

assessed in the context of the military's  
more traditional role of protecting the  
nation.

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## Managing the Downsized and Restructured Force

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In response to budget constraints and a decreased post-Cold War threat, difficult decisions must be made about how best to structure, train, support, and maintain a smaller, increasingly U.S.-based force so it is highly ready, sustainable, and capable of responding to a crisis on short notice. DOD's challenge will be to maintain high levels of military capability while at the same time significantly reducing the number of both military and civilian positions.

To implement the new security strategy announced in February 1991, DOD has developed a base force concept, which calls for a reduction in military forces by 25 percent by 1997. The Congress will likely debate whether further cuts in military forces below the base force are possible because of the decline in the Soviet threat. A major concern is whether further cuts will result in a repetition of the "hollow Army" of the 1970s and will leave the United States unable to effectively protect national security interests in a still dangerous world. Policymakers will have to balance these concerns as forces are eliminated and restructured and capabilities are assessed against potential regional threats.

A key issue in the defense arena will be how many and what kinds of forces should make up U.S. military forces. In particular, scrutiny should be given to the mix of active and reserve forces. Consideration needs to be given to whether (1) certain missions can be transferred from the active forces to the less expensive reserves, (2) a greater number of support forces are needed in the active forces, and (3) some reserve units are not needed and can be deactivated. At the same time, the Army could expand the use of certain reserve support forces in its contingency force and should examine each of the elements of the force structure being withdrawn from Europe to determine whether any of these units' missions could be shifted to the reserves.

Furthermore, in light of the Gulf War and the new security environment, sustaining U.S. forces will require a reexamination of critical issues. DOD's forces must be restructured and reduced without sacrificing the U.S. capacity to respond in time of crisis. Key issues include

- the capability for airlift and sealift that is needed to quickly respond to regional crises anywhere in the world,

- the need to continue existing land and sea prepositioning strategies,
- the extent to which high levels of readiness and overall military capability are being maintained, and
- the extent to which U.S. forces will depend on support and sustainability resources from allies.

Planning for and managing reductions in the number of civilian and military personnel and their accompanying adjustment and assistance programs will also be of critical importance. DOD is just over halfway toward meeting its goal of eliminating nearly 800,000 active duty and civilian jobs from the peak strength levels it reached in fiscal year 1987. Further reductions are expected as a result of additional base closures and other budgetary trade-offs. These cuts will continue to affect local communities and military and civilian personnel who are making the transition into the civilian work force. The Congress has authorized special funding for community adjustment and assistance programs. Our work indicates that DOD needs better plans for reducing its work force, especially its civilian work force, to ensure it retains the right skills.

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# Reassessing U.S. Commitments, Forward Presence, and Security Assistance Programs

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The end of the Cold War requires a reassessment of the U.S. military presence overseas, of host government contributions to the United States for maintaining its forces, and of military assistance programs provided to U.S. allies. DOD proposes cutting forces in Europe from over 300,000 in 1989 to 150,000 by 1995. The Congress has mandated deeper cuts, down to 100,000, by 1996. Determining the right size and composition of overseas forces will be a major challenge. U.S. forces stationed in Europe and the Far East will be affected by such factors as threats, allied capabilities, new status of forces agreements, and the willingness of allies to increase their contributions to the defense burden. The North Atlantic Treaty Organization (NATO) is reconsidering its mission and structure and the future role of U.S. forces. Also, proposed changes to the NATO members' status of forces agreement with Germany could directly affect the training and operational readiness of U.S. and other NATO forces. These new changes will influence decisions affecting the size and composition of U.S. forces deployed to Europe. Similar concerns must be addressed for U.S. forces stationed in the Far East.

Congressional concerns about increased allied burden sharing will continue. Our work in NATO, Japan, and Korea shows there are further opportunities for host country contributions to the United States to offset the costs of stationing U.S. forces. For example, increases in South Korea's contributions for depot maintenance, war reserves, indigenous labor, and military construction could save the United States \$500 million or more annually.

U.S. security assistance programs, including foreign military equipment sales, training, and economic support fund activities, provided billions of dollars to foreign countries during the Cold War. The fall of the Berlin Wall, the communists' loss of power in Central and Eastern Europe, and the dissolution of the Soviet Union have eliminated the Cold War rationale for the U.S. foreign assistance programs. The radically changed environment has resulted in some modification to security assistance goals, with new or added focus on providing aid for establishing democratic institutions and civilian control over the military, on stabilizing regional tensions, and on combating illegal drug trafficking.

While there have been some changes in our security assistance programs, we recently reported that a limited number of traditional recipients continue to receive the majority of security assistance. The two main recipients, Israel and Egypt, have been provided massive economic and military aid since the Camp David agreements in 1978, which among other things, called for a peace treaty between the two countries. Rounding out the top six recipients are Greece, Turkey, Portugal, and the Philippines, all receiving substantial security assistance funds as part of their base rights agreements with the United States. Even though bases in the Philippines were recently closed, in fiscal year 1993 these six countries will receive \$6.2 billion, or 83 percent, of the total \$7.5 billion in U.S. security assistance funding.

The challenge to the Congress and the new administration will be to determine U.S. security priorities and the corresponding size and shape of a security assistance program that will be flexible and adaptable in a world with divergent regional threats.

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# Controlling the Spread of Weapons of Mass Destruction

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Concerns about the effectiveness of existing controls over the proliferation of weapons of mass destruction have been heightened by post-Gulf War revelations about Iraq's nuclear weapons program, uncertainty over the security of nuclear weapons material in the former Soviet Union, and Chinese transfers of nuclear and missile technology to the Middle East. These events highlight shortcomings in the international community's ability to detect clandestine weapons programs and control the transfer of the equipment, material, and technology necessary for weapons proliferation. Halting weapons proliferation in the 1990s will require increased international cooperation to strengthen verification of existing agreements, to control international technology transfers, and to dispose of Cold War nuclear and chemical weapons stockpiles in the former Soviet Union. Through various programs and initiatives managed by the Departments of State, Defense, Commerce, and Energy and the Arms Control and Disarmament Agency, the United States has an important leadership role to play in each of these areas.

The new administration and the Congress will face difficult issues concerning the existing nonproliferation treaties and

regimes such as the Nuclear Nonproliferation Treaty, the Missile Technology and Control Regime, and the Australia Group on chemical weapons. Among these issues are (1) how to increase participation in these regimes by potential "problem states," (2) whether to adopt more intrusive verification procedures to determine compliance, and (3) how to strengthen enforcement. Policymakers will also have to determine how best to help former Soviet republics in the timely dismantlement of their nuclear and chemical weapons and missile delivery systems. Although more than \$800 million has been authorized to assist this effort, it is unclear whether the funded activities will accelerate the dismantling process.

To improve the effectiveness of export controls in this changing security environment, the U.S. government first needs to continue its efforts to strengthen multilateral export control regimes, to include initiatives to broaden participation, and to coordinate and share information about export control decisions. On a bilateral basis, the United States should also work with the states of the former Soviet Union and the Warsaw Pact to ensure that

they set up and maintain effective export control systems.

The Departments of Commerce, State, and Defense, with input from the intelligence community and the Department of Energy, all have responsibilities for developing and administering controls over dual-use items—those with both military and civilian uses. Similarly, two agencies—the Commerce Department and the Customs Service—share primary responsibility for preventing or detecting the illegal export of controlled items. This is an appropriate time for the administration to reassess the roles of these agencies and the various interagency coordinating mechanisms that are currently in place.

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# Reforming Weapons System Acquisition While Preserving the Industrial Base

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The research, development, and procurement of weapons systems account for about 30 percent of all defense spending. DOD is pursuing close to 100 major weapons system acquisitions at a projected research, development, and procurement cost of over \$1 trillion. Over the years, such expenditures have produced many of the world's most technologically advanced and capable weapons systems. Nevertheless, the manner and process in which weapons requirements are determined and weapons are acquired have often proved costly and inefficient—if not wasteful. The combination of unrealistic spending plans, costly weapons requirements, overly optimistic cost estimates, and high-risk acquisition schedules has resulted in an annual budget cycle of weapons cost overruns that require increased funding or program adjustments that reduce, delay, and/or stretch out the programs.

A gap between DOD's future year spending plan and available funds amounts to billions of dollars. DOD's tendency to overestimate the amount of future funding available for planned programs and the agency's tendency to underestimate program costs result in more programs being started than can be executed. DOD's attempts to narrow the

planning-funding mismatch will be hampered if assumed savings are not realized and program costs increase beyond planned levels—a historically frequent occurrence. For example, DOD's projected savings of over \$100 billion from weapons systems terminations and new acquisition approaches has been reduced by \$12 billion in programs restored by Congress and \$5.4 billion for defense conversions to commercial activities. Greater defense funding cuts will further hurt efforts to bring plans in line with funding levels and will seriously challenge policymakers in determining how many weapons programs we can afford.

Past efforts to reform the acquisition process have not eliminated these problems. A prevailing culture that depends on generating and supporting new weapons acquisitions has defeated past reform efforts. DOD must rededicate its efforts to improving weapons acquisition. This will require top management commitment and further movement toward centralized management and consolidation of acquisition roles, missions, and support functions. Clear accountability for implementing reforms is also critical.

Overpriced defense contracts and improper influence in the contracting process are two highly vulnerable areas subject to fraud and abuse. Vulnerabilities related to inadequate cost estimating, defective pricing, and improper contracting practices cost the taxpayers billions of dollars more than necessary for goods and services purchased.

Details on our concerns about DOD's annual expenditure of billions of dollars on weapons system research, development, acquisition, and vulnerability to contract fraud and abuse are available in our high-risk reports.

As the defense budget is reduced, policymakers will face a number of critical issues related to preserving technological leadership and ensuring the existence of the industrial base capabilities required to meet U.S. national security needs. The issues include (1) defense industrial restructuring and adjustment to a declining defense market; (2) the impact of relying on foreign sources for critical technology and products to meet defense needs; (3) the impact of foreign investment in key industries supporting defense; (4) and the impact on U.S. competitiveness of technology transfer to other countries through various

government programs, including arms sales and weapons coproduction agreements. Our work shows that DOD needs to take a more active role regarding each of these issues.

DOD has taken the position that free market forces generally will guide the restructuring of the defense industrial base. The agency has also stated that its ability to meet future national security needs will depend largely on the ability of individual companies to shift from defense to commercial production and then back again, as required. DOD should adopt a more realistic strategy for ensuring that government decisions and industry adjustments will result in the industrial and technological capabilities needed to meet future U.S. national security requirements. The current strategy does not adequately recognize that DOD will continue to make budget and contract award decisions worth many billions of dollars annually to develop and acquire weapons and other military equipment. These decisions greatly affect, directly and indirectly, the structure of the defense industrial base.

In addition, free market restructuring is often motivated by short-term considerations such as profit, rather than by considerations of how well the changes in

the defense industry will serve long-term U.S. national security needs. Moreover, many defense companies may lack the experience and specialized knowledge to shift to commercial production successfully. In May 1992, DOD reiterated its free market strategy but stated its intention to assess and monitor the industrial base and to take action to preserve a needed critical capability in those "exceptional situations" when the capability may be lost and cannot be recovered in time to meet an emerging threat. It remains to be seen how well this approach will be implemented. However, unless DOD takes a more active role than it currently envisions in ensuring the existence of the critical capabilities most likely to be needed in the future, it risks losing these capabilities.

DOD also needs to take a more active role in assessing U.S. reliance on foreign sources and foreign investment relating to the defense industrial base. DOD has not systematically maintained data on firms that provide specialized technology to meet its critical needs. As a result, DOD generally does not know the extent to which it uses or depends on foreign technology and products to meet such needs. DOD also lacks agreed-upon criteria for assessing the

national security risks posed by dependencies. The lack of criteria impairs the ability of DOD to determine the actions it could or should take to reduce these risks. In addition, no federal agency or process systematically tracks foreign investment in companies that are primarily commercial but whose leading-edge technologies are important to U.S. leadership in defense technologies.

Similarly, DOD and other agencies involved in technology transfer programs, such as arms sales, coproduction, and codevelopment, need to place a higher priority on determining the long-term impact of such activities on U.S. competitiveness and the industrial base. No government entity collects data on these arrangements, even though many of these activities are believed to adversely affect the competitive position of U.S. companies and possibly to undermine U.S. security interests.

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# Addressing Environmental Challenges

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DOD faces several environmental challenges in the 1990s. In addition to having to comply with U.S. and foreign environmental requirements, to minimize pollution, and to comply with clean air and water legislation, DOD is confronted with a major task—cleaning up hazardous wastes. The annual cost of this task has increased from \$86 million in 1984 to an estimated \$1.6 billion in 1993. DOD does not know how much cleaning up environmental damage will cost. Estimates have increased to \$24.5 billion from the \$5 billion to \$10 billion anticipated in 1985. This latest estimate is likely to increase because DOD has not yet identified all of the contaminated sites and the extent of contamination to be cleaned up.

DOD has made significant strides in its recognition of such problems and in its efforts to address them. The increasing resources DOD devotes to cleaning up its contaminated areas and its initiatives to reduce pollution from current operations and weapons systems signal a new cultural attitude. The improvements notwithstanding, we believe that DOD does not yet fully recognize the magnitude of the task before it, including long-term cleanup costs.

One key to success in meeting this challenge will be information—on the nature of the pollution that must be cleaned up, on the location of the contamination, on the technologies available to do the job, on the costs of remedial actions, and on the progress of cleanup programs. We recently reported on the lack of sufficient information on, for example, DOD's underground storage tanks and the costs of reimbursing contractors for cleanup efforts. As an initial priority, DOD needs to consider the types of information needed by its decisionmakers and improve the availability and quality of such data.

Another issue facing DOD is the destruction of existing stockpiles of chemical weapons. Estimates to dispose of these weapons have increased from \$1.7 billion in 1985 to almost \$8 billion as of March 1992. DOD recently advised the Congress that additional costs should be expected.

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## Following Through on Inventory and Other Management Initiatives

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DOD is one of the largest, most diverse, and most complex organizations in the world. Over the years, DOD has responded to external and internal calls for streamlining its organization and for promoting efficiency and effectiveness. The 1986 Goldwater-Nichols Act can be credited for, among other things, the increased coordination that is beginning to become apparent within the military establishment—as witnessed, for example, in the successful joint operations in the Persian Gulf. At about the same time, the Packard Commission came out with a report whose recommendations sparked a series of efforts aimed at improving the Department's organization and management. The Defense Management Review report, issued in July 1989, is intended to address a number of actions to modernize the Department's operations and to save substantial sums, while maintaining the essential strength and readiness of the armed services. Following through with these initiatives must remain a high priority if promised savings are to be achieved.

The sheer size of the Department, coupled with the complexity of its programs and components, presents a Herculean challenge to those charged with substantially

improving Defense management overall. One of the main issues involves developing and fostering changes in management philosophy and organizational culture. An organization's culture has a strong influence on the behavior of its members and the success of the organization as a whole. Improvements in the area of inventory management, for example, will depend in large measure on leadership-inspired cultural changes, such as going from a "having more is always better" way of thinking to a "having what is needed when and where it is needed" philosophy.

DOD's supply inventory contained millions of items worth close to \$100 billion as of September 30, 1991. We estimate the cost of excess supplies is \$40 billion. In the past, DOD has not emphasized economy and efficiency in purchasing, maintaining, and distributing these supplies. However, it has recently initiated some projects based on the use of commercial distribution systems and other commercial practices to address these problems. These efforts need to be expanded throughout the supply chain. Even then, they will not be fully successful until DOD puts in place computer and data systems to aid in managing the supply system. Sustained top management commitment to fixing inventory management problems is critical. For a

further discussion of inventory management problems, see our high-risk report.

Another DOD initiative involves the consolidation of supply depots under the Defense Logistics Agency. If properly combined with other Department initiatives, this effort could result in more efficient and cost-effective operations. However, consolidation alone will not achieve these objectives unless it is accompanied by a stock positioning plan that is well thought out—one that takes into account the impact of the inventory reduction plan, of the reduced demand caused by reductions in the military force structure, and of the inventory reductions associated with adopting commercial “quick response” practices.

Another initiative is the improvement of DOD’s business processes, such as financial and personnel management, through the establishment of the Corporate Information Management (CIM) System. This initiative is expected to provide about \$36 billion in savings. In the short term, the CIM system is to reduce or eliminate information systems that perform the same function. In the longer term, the CIM system is to (1) implement new or improved business practices (in, for example, the way DOD buys and distributes

supplies); (2) create uniform business processes for common functions; (3) improve the standardization, quality, and consistency of data from defense management information systems; and (4) develop standard information systems to meet common functional requirements. On the basis of DOD's past experience, we believe it will be difficult to achieve the savings promised by the CIM system.

In addition, DOD is projecting \$5 billion in savings in the next 5 years as a result of base closures. Our work, however, raises serious questions on whether these savings will be realized.

The Defense Business Operations Fund was established in fiscal year 1992 to place industrial funds, stock funds, and other defense support functions under centralized overview and control. DOD estimates that the Fund will have sales of goods and services of about \$81 billion in fiscal year 1993. Two of the basic objectives of this initiative are to capture all the costs of operating a business area and to charge customers the actual cost of the goods and services they received. While achieving these objectives could establish a more businesslike operation, key policies and systems involving standard cost

accounting, rate-setting, cash management, capital asset accounting, and intrafund transactions have not yet been fully developed. DOD must strongly commit itself to managing the Fund if the potential financial and management benefits are to be achieved.

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# Improving Financial Management

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To control costs, it is first necessary for managers to determine what the costs are. Currently, DOD is unable to do this for many of its activities because its financial systems and practices are out of date, inaccurate, and unreliable. Consequently, the kind of relevant, credible financial information that program managers, commanders, and top executives need to reduce costs and measure performance is often not available.

Achieving compliance with the Chief Financial Officers' Act of 1990 (which the Congress enacted to improve financial management governmentwide) could significantly help DOD reach its goals. The act's provisions are consistent with DOD's financial initiatives. The act further requires financial audits for numerous government activities that control hundreds of billions of dollars in assets. However, our recent financial audits of the Air Force and the Army have shown that the military services are still unable to produce financial statements that are sufficiently reliable for an auditor to express an opinion on them. For example, we identified over \$200 billion in adjustments needed to improve the accuracy of Army and Air Force financial reporting. Accordingly, the statements'

usefulness to government decisionmakers and the public is therefore limited.

DOD is primarily relying on long-term initiatives to provide solutions to its financial management problems. However, DOD also needs to make short-term improvements in internal controls and in the quality of financial data in its existing systems. Making fundamental, comprehensive improvements in DOD's financial operations will require personnel at all levels to adopt priorities and business practices that have not previously been in place within DOD. Changes on this scale will require sustained personal attention and leadership from top officials, including the Secretary of Defense, and a willingness to look beyond DOD to supplement its existing financial management expertise.

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## Related GAO Products

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Acquisition Management: A Rare Opportunity for Lasting Change  
(GAO/NSIAD-93-15, forthcoming).

Defense Contract Pricing (GAO/HR-93-8,  
Dec. 1992).

Defense Inventory Management (GAO/HR-93-12,  
Dec. 1992).

Defense Weapons System Acquisition  
(GAO/HR-93-7, Dec. 1992).

Triad Project Summary (GAO/PEMD-92-36R,  
Sept. 28, 1992).

Financial Management: Immediate Actions Needed to Improve Army Financial Operations and Controls (GAO/AFMD-92-82,  
Aug. 7, 1992).

Russian Nuclear Weapons: U.S. Implementation of the Soviet Nuclear Threat Reduction Act of 1991 (GAO/T-NSIAD-92-47,  
July 27, 1992).

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