



## Testimony

Before the Subcommittee on Terrorism,  
Unconventional Threats and Capabilities,  
Committee on Armed Services, U.S. House of  
Representatives

---

For Release on Delivery  
Expected at time 1:30 p.m.  
Wednesday, March 31, 2004

# DEPARTMENT OF DEFENSE

## Further Actions Needed to Establish and Implement a Framework for Successful Business Transformation

Statement of Gregory D. Kutz  
Director, Financial Management and Assurance

Randolph C. Hite  
Director, Information Technology Architecture and  
Systems



G A O

Accountability \* Integrity \* Reliability

---

---

---

This is a work of the U.S. government and is not subject to copyright protection in the United States. It may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.

---

DEPARTMENT OF DEFENSE

Further Actions Needed to Establish and Implement a Framework for Successful Business Transformation



Highlights of GAO-04-626T, a testimony before the Subcommittee on Terrorism, Unconventional Threats and Capabilities, Committee on Armed Services, U.S. House of Representatives

Why GAO Did This Study

GAO has issued several reports pertaining to the Department of Defense's (DOD) architecture and systems modernization efforts which revealed that many of the underlying conditions that contributed to the failure of prior DOD efforts to improve its business systems remain fundamentally unchanged. The Subcommittee asked GAO to provide its perspectives on (1) the impact long-standing financial and related business weaknesses continue to have on DOD, (2) the underlying causes of DOD business transformation challenges, and (3) DOD business transformation efforts. In addition, GAO reiterates the key elements to successful reform: (1) an integrated business transformation strategy, (2) sustained leadership and resource control, (3) clear lines of responsibility and accountability, (4) results-oriented performance, (5) appropriate incentives and consequences, (6) an enterprise architecture to guide reform efforts, and (7) effective monitoring and oversight. GAO also offers two suggestions for legislative consideration that are intended to improve the likelihood of meaningful, broad-based financial management and related business reform at DOD.

[www.gao.gov/cgi-bin/getrpt?GAO-04-626T](http://www.gao.gov/cgi-bin/getrpt?GAO-04-626T).

To view the full product, including the scope and methodology, click on the link above. For more information, contact Gregory Kutz at (202) 512-9095 or (kutzg@gao.gov) or Randolph Hite, (202) 512-3439

What GAO Found

DOD's senior civilian and military leaders are committed to transforming the department and improving its business operations and have taken positive steps to begin this effort. However, overhauling the financial management and related business operations of one of the largest and most complex organizations in the world represents a huge management challenge. Six DOD program areas are on GAO's "high risk" list, and the department shares responsibility for three other governmentwide high-risk areas. DOD's substantial financial and business management weaknesses adversely affect not only its ability to produce auditable financial information, but also to provide timely, reliable information for management and Congress to use in making informed decisions. Further, the lack of adequate transparency and appropriate accountability across all of DOD's major business areas results in billions of dollars in annual wasted resources in a time of increasing fiscal constraint.

Impact of Weaknesses in Human Capital Management, Internal Control, and Systems

Business area affected	Problem identified
Military pay	Ninety-four percent of mobilized Army National Guard soldiers GAO investigated had pay problems. These problems distracted soldiers from their missions, imposed financial hardships on their families, and had a negative impact on retention.
Logistics	Asset visibility and other logistical support problems hampered mission readiness during Operation Iraqi Freedom, including cannibalization of vehicles for parts and duplication of requisitions.
Travel	Seventy-two percent of the over 68,000 premium class airline tickets DOD purchased for fiscal years 2001 and 2002 were not properly authorized and 73 percent were not properly justified.
Property	New JSLIST chem-bio suits sold on the Internet for \$3 while at the same time DOD was buying them for over \$200. Further, thousands of defective suits, declared excess by DOD, were improperly issued to local law enforcement agencies—which are likely to be first responders in case of a terrorist attack.
Contract payments	Some DOD contractors were abusing the federal tax system, with little or no consequence. As of September 2003, DOD had collected only \$687,000 of unpaid federal taxes through a mandated levy program. GAO estimated that at least \$100 million could be collected annually through effective implementation of the levy on DOD contract payments.

Source: GAO.

Four underlying causes impede reform: (1) lack of sustained leadership, (2) cultural resistance to change, (3) lack of meaningful metrics and ongoing monitoring, and (4) inadequate incentives and accountability mechanisms. To address these issues, GAO reiterates the keys to successful business transformation and offers two suggestions for legislative action. First GAO suggests that a senior management position be established to spearhead DOD-wide business transformation efforts. Second, GAO proposes that the leaders of DOD's functional areas, referred to as departmentwide domains, receive and control the funding for system investments, as opposed to the military services. Domain leaders would be responsible for managing business system and process reform efforts within their business areas and would be accountable to the new senior management official for ensuring their efforts comply with DOD's business enterprise architecture.

Mr. Chairman and Members of the Subcommittee:

It is a pleasure to be here to discuss key aspects of business transformation efforts at the Department of Defense (DOD). At the outset, we would like to thank the Subcommittee for having this hearing and acknowledge the important role hearings such as this one serve. The involvement of this Subcommittee is critical to ultimately assuring public confidence in DOD as a steward that is accountable for its finances. DOD's substantial long-standing business management systems and related problems adversely affect the economy, effectiveness, and efficiency of its operations, and have resulted in a lack of adequate transparency and appropriate accountability across all major business areas. As a result, DOD does not have timely, reliable information for management to use in making informed decisions. Further, as our reports continue to show, these problems result in significant fraud, waste, and abuse and hinder DOD's attempts to develop world-class operations and activities to support its forces. Of the 25 areas on GAO's governmentwide "high risk" list, 6 are DOD program areas, and the department shares responsibility for 3 other high-risk areas that are governmentwide in scope.<sup>1</sup> The problems we continue to identify relate to human capital challenges, ineffective internal control and processes, and duplicative and stovepiped business systems. The seriousness of DOD's business management weaknesses underscores the importance of no longer condoning "status quo" business operations at DOD.

Over the last 3 years, DOD has taken action to begin addressing a number of these challenges as part of its business transformation effort. Business transformation has been a priority of Secretary Rumsfeld. For example, DOD has been granted additional human capital flexibilities and is in the process of developing a new personnel management system for its civilian employees. In addition, through its Business Management Modernization Program (BMMP), DOD is continuing its efforts to develop and implement a business enterprise architecture and establish effective management and control over its business system modernization investments. To date, however, the underlying operational conditions remain fundamentally unchanged and

---

<sup>1</sup> U.S. General Accounting Office, *High-Risk Series: An Update*, GAO-03-119 (Washington, D.C.: January 2003). The nine interrelated high-risk areas that represent the greatest challenge to DOD's development of world-class business operations to support its forces are: contract management, financial management, human capital management, information security, support infrastructure management, inventory management, real property,

tangible evidence of improvements in DOD business operations remains limited to specific business process areas, such as DOD's purchase card program, where improvements have generally resulted from increased management focus and better internal control rather than from major modifications to automated systems. It is important to note that some of the key elements we highlight in this testimony as necessary for successful business transformation were critical to the success of several of the interim initiatives that we will discuss today.

Because DOD is one of the largest and most complex organizations in the world, overhauling its business operations represents a huge management challenge. In fiscal year 2003, DOD reported that its operations involved over \$1 trillion in assets, nearly \$1.6 trillion in liabilities, approximately 3.3 million military and civilian personnel, and disbursements of over \$416 billion. Moreover, execution of DOD operations spans a wide range of defense organizations, including the military services and their respective major commands and functional activities, numerous large defense agencies and field activities, and various combatant and joint operational commands that are responsible for military operations for specific geographic regions or theaters of operations. To execute these military operations, the department performs an assortment of interrelated and interdependent business process areas, including logistics management, procurement, healthcare management, and financial management. Secretary Rumsfeld has estimated that successful improvements to DOD's business operations could save the department 5 percent of its budget a year. Using DOD's reported fiscal year 2004 budget authority amounts, this percentage would equate to approximately \$22 billion a year in savings.

Over the last 3 years, we have made a series of recommendations to DOD and suggestions for legislative changes that provide a framework for effectively addressing the challenges DOD faces in transforming its financial management and related business operations and systems and offered several key elements necessary for reform to succeed.<sup>2</sup> This framework recognizes the

---

systems modernization, and weapon systems acquisition.

<sup>2</sup> U.S. General Accounting Office, *DOD Financial Management: Integrated Approach, Accountability, Transparency, and Incentives Are Keys to Effective Reform*, GAO-02-497T (Washington, D.C.: Mar. 6, 2002), U.S. General Accounting Office, *Information Technology: Architecture Needed to Guide Modernization of DOD's Financial Operations*, GAO-01-525 (Washington, D.C.: May 17, 2001), U.S. General Accounting Office, *DOD Business Systems Modernization: Improvements to Enterprise Architecture Development and Implementation Efforts Needed*, GAO-03-458 (Washington, D.C.: Feb. 28, 2003), U.S. General Accounting Office, *DOD Business Systems Modernization: Continued Investment in Key Accounting Systems Needs to be Justified*, GAO-03-465

complexity of the challenge and the long-term nature of overcoming it. Moreover, it recognizes the underlying causes of the challenge, such as lack of sustained leadership, cultural resistance to change, parochialism, and stovepiped operations, that impeded the success of previous administrations in addressing DOD's problems that continue today. DOD has agreed with our recommendations and launched efforts intended to implement them, but progress has been slow. If DOD is unable to address these underlying causes that have resulted in the failure of previous broad-based reform efforts, improvements will remain marginal, confined to narrowly defined business process areas and incremental improvements in human capital policies, business processes, internal control systems, and information technologies.

Today, we will provide our perspectives on (1) the impact that long-standing financial management and related business process weaknesses continue to have on DOD, (2) underlying causes that have impeded the success of prior efforts, (3) keys to successful reform, and (4) DOD's business transformation efforts. In addition, we will offer two suggestions for legislative consideration, which we believe will provide the sustained top-level leadership and accountability necessary for the business transformation effort to succeed. Our statement is based on previous GAO reports as well as on our review of the work of other DOD auditors and recent DOD reports and studies.

## **Impact of Financial Management and Related Business Process Weaknesses**

For several years we have reported that DOD faces a range of financial management and related business process challenges that are complex, long-standing, pervasive, and deeply rooted in virtually all business operations throughout the department. As the Comptroller General recently testified and as discussed in our latest financial audit report,<sup>3</sup> DOD's financial management

---

(Washington, D.C.: March 28, 2003) and *DOD Business Systems Modernization: Longstanding Management and Oversight Weaknesses Continue to Put Investments at Risk*, GAO-03-553T (Washington, D.C.: Mar. 31, 2003), U.S. General Accounting Office, *Business Systems Modernization: Summary of GAO's Assessment of the Department of Defense's Initial Business Enterprise Architecture*, GAO-03-877R (Washington, D.C.: July 7, 2003), and U.S. General Accounting Office, *DOD Business Systems Modernization: Important Progress Made to Develop Business Enterprise Architecture, but Much Work Remains*, GAO-03-1018 (Washington, D.C.: Sept. 19, 2003).

<sup>3</sup> U.S. General Accounting Office, *Fiscal Year 2003 U.S. Government Financial Statements: Sustained Improvement in Federal Financial Management Is Crucial to Addressing Our Nation's Future Fiscal Challenges*, GAO-04-477T

deficiencies, taken together, continue to represent the single largest obstacle to achieving an unqualified opinion on the U.S. government's consolidated financial statements. To date, none of the military services has passed the test of an independent financial audit because of pervasive weaknesses in internal control and processes and fundamentally flawed business systems.

In identifying improved financial performance as one of its five governmentwide initiatives, the President's Management Agenda recognized that obtaining a clean (unqualified) financial audit opinion is a basic prescription for any well-managed organization. At the same time, it recognized that without sound internal control and accurate and timely financial and performance information, it is not possible to accomplish the President's agenda and secure the best performance and highest measure of accountability for the American people. The Joint Financial Management Improvement Program (JFMIP)<sup>4</sup> principals have defined certain measures, in addition to receiving an unqualified financial statement audit opinion, for achieving financial management success. These additional measures include (1) being able to routinely provide timely, accurate, and useful financial and performance information, (2) having no material internal control weaknesses or material noncompliance with laws and regulations, and (3) meeting the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA).<sup>5</sup> Unfortunately, DOD does not meet any of these conditions. For example, for fiscal year 2003, the DOD Inspector General (DOD IG) issued a disclaimer of opinion on DOD's financial statements, citing 11 material weaknesses in internal control and noncompliance with FFMIA requirements.

Recent audits and investigations by GAO and DOD auditors continue to confirm the existence of pervasive weaknesses in DOD's financial management and related business processes and systems. These problems have (1) resulted in a lack of reliable information needed to make

---

(Washington, D.C.: Mar. 3, 2004) and our report contained in the U.S. Department of the Treasury, *Financial Report of the United States Government* (Washington, D.C.: Feb. 27, 2004).

<sup>4</sup> JFMIP is a joint undertaking of the Office of Management and Budget, GAO, the Department of Treasury, and the Office of Personnel Management, working in cooperation with each other and with operating agencies to improve financial management practices throughout the government.

<sup>5</sup> FFMIA, Pub. L. No. 104-208, Div. A., title VIII, 110 Stat. 3009-389—3009-393, Sept. 30, 1996, requires the 23 major departments and agencies covered by the Chief Financial Officers Act of 1990, Pub. L. No. 101-576, 104 Stat. 2838, Nov. 15, 1990 (as amended), to implement and maintain financial management systems that comply substantially with (1) federal financial management systems requirements, (2) applicable federal accounting standards, and (3) *U.S. Standard General Ledger (SGL)* at the transaction level.

sound decisions and report on the status of DOD activities, including accountability of assets, through financial and other reports to Congress and DOD decision makers, (2) hindered its operational efficiency, (3) adversely affected mission performance, and (4) left the department vulnerable to fraud, waste, and abuse. For example,

- 450 of the 481 mobilized Army National Guard soldiers from six GAO case study Special Forces and Military Police units<sup>6</sup> had at least one pay problem associated with their mobilization. DOD's inability to provide timely and accurate payments to these soldiers, many of whom risked their lives in recent Iraq or Afghanistan missions, distracted them from their missions, imposed financial hardships on the soldiers and their families, and has had a negative impact on retention. (GAO-04-89, Nov. 13, 2003)
- DOD incurred substantial logistical support problems as a result of weak distribution and accountability processes and controls over supplies and equipment shipments in support of Operation Iraqi Freedom activities, similar to those encountered during the prior gulf war. These weaknesses resulted in (1) supply shortages, (2) backlogs of materials delivered in theater but not delivered to the requesting activity, (3) a discrepancy of \$1.2 billion between the amount of materiel shipped and that acknowledged by the activity as received, (4) cannibalization of vehicles, and (5) duplicate supply requisitions. (GAO-04-305R, Dec. 18, 2003)
- Inadequate asset visibility and accountability resulted in DOD selling new Joint Service Lightweight Integrated Suit Technology (JSLIST)—the current chemical and biological protective garment used by our military forces—on the internet for \$3 each (coat and trousers) while at the same time buying them for over \$200 each. DOD has acknowledged that these garments should have been restricted to DOD use only and

---

<sup>6</sup> The six case study units reviewed include the Colorado B Company, Virginia B Company, West Virginia C Company, Mississippi 114<sup>th</sup> Military Police Company, California 49<sup>th</sup> Military Police Headquarters and Headquarters Detachment, and the Maryland 200<sup>th</sup> Military Police Company. In addition, our limited review of pay experiences of soldiers in the Colorado Army Guard's 220<sup>th</sup> Military Police Company, who recently returned from Iraq, indicated that some of the same types of pay problems that we found in our case studies had also affected them.



therefore should not have been available to the public. (GAO-02-873T, June 25, 2002)

- Inadequate asset accountability also resulted in DOD's inability to locate and remove over 250,000 defective Battle Dress Overgarments (BDOs)—the predecessor of JSLIST—from its inventory. Subsequently, we found that DOD had sold many of these defective suits to the public, including 379 that we purchased in an undercover operation. In addition, DOD may have issued over 4,700 of the defective BDO suits to local law enforcement agencies. Although local law enforcement agencies are most likely to be the first responders to a terrorist attack, DOD failed to inform these agencies that using these BDO suits could result in death or serious injury. (GAO-04-15NI, Nov. 19, 2003)
- Tens of millions of dollars are not being collected each year by military treatment facilities from third-party insurers because key information required to effectively bill and collect from third-party insurers is often not properly collected, recorded, or used by the military treatment facilities. (GAO-04-322R, Feb. 20, 2004)
- Our analysis of data on more than 50,000 maintenance work orders opened during the deployments of six battle groups indicated that about 29,000 orders (58 percent) could not be completed because the needed repair parts were not available on board ship. This condition was a result of inaccurate ship configuration records and incomplete, outdated, or erroneous historical parts demand data. Such problems not only have a detrimental impact on mission readiness, they may also increase operational costs due to delays in repairing equipment and holding unneeded spare parts inventory. (GAO-03-887, Aug. 29, 2003)
- DOD sold excess biological laboratory equipment, including a biological safety cabinet, a bacteriological incubator, a centrifuge, and other items that could be used to produce biological warfare agents. Using a fictitious company and fictitious individual identities, we were able to purchase a large number of new and usable

equipment items over the Internet from DOD. Although the production of biological warfare agents requires a high degree of expertise, the ease with which these items were obtained through public sales increases the risk that terrorists could obtain and use them to produce biological agents that could be used against the United States. (GAO-04-81TNI, Oct. 7, 2003)

- Based on statistical sampling, we estimated that 72 percent of the over 68,000 premium class airline tickets DOD purchased for fiscal years 2001 and 2002 was not properly authorized and that 73 percent was not properly justified. During fiscal years 2001 and 2002, DOD spent almost \$124 million on premium class tickets that included at least one leg in premium class—usually business class. Because each premium class ticket cost the government up to thousands of dollars more than a coach class ticket, unauthorized premium class travel resulted in millions of dollars of unnecessary costs being incurred annually. (GAO-04-229T, Nov. 6, 2003)
- Some DOD contractors have been abusing the federal tax system with little or no consequence, and DOD is not collecting as much in unpaid taxes as it could. Under the Debt Collection Improvement Act of 1996, DOD is responsible—working with the Treasury Department—for offsetting payments made to contractors to collect funds owed, such as unpaid federal taxes. However, we found that DOD had collected only \$687,000 of unpaid taxes as of September 2003. We estimated that at least \$100 million could be collected annually from DOD contractors through effective implementation of levy and debt collection programs. (GAO-04-95, Feb. 12, 2004)
- Our review of fiscal year 2002 data revealed that about \$1 of every \$4 in contract payment transactions in DOD’s Mechanization of Contract Administration Services (MOCAS) system was for adjustments to previously recorded payments—\$49 billion of adjustments out of \$198 billion in disbursement, collection, and adjustment transactions. According to DOD, the cost of researching and making adjustments to

accounting records was about \$34 million in fiscal year 2002, primarily to pay hundreds of DOD and contractor staff. (GAO-03-727, Aug. 8, 2003)

- DOD's information technology (IT) budget submission to Congress for fiscal year 2004 contained material inconsistencies, inaccuracies, or omissions that limited its reliability. For example, we identified discrepancies totaling about \$1.6 billion between two primary parts of the submission—the IT budget summary report and the detailed Capital Investments Reports on each IT initiative. These problems were largely attributable to insufficient management attention and limitations in departmental policies and procedures, such as guidance in DOD's Financial Management Regulation, and to shortcomings in systems that support budget-related activities. (GAO-04-115, Dec. 19, 2003)
- Since the mid 1980s, we have reported that DOD uses overly optimistic planning assumptions to estimate its annual budget request. These same assumptions are reflected in its Future Years Defense Program, which reports projected spending for the current budget year and at least 4 succeeding years. In addition, in February 2004 the Congressional Budget Office projected that DOD's demand for resources could grow to about \$490 billion in fiscal year 2009. DOD's own estimate for that same year was only \$439 billion.<sup>7</sup> As a result of DOD's continuing use of optimistic assumptions, DOD has too many programs for the available dollars, which often leads to program instability, costly program stretch-outs, and program termination. Over the past few years, the mismatch between programs and budgets has continued, particularly in the area of weapons systems acquisition. For example, in January 2003, we reported that the estimated costs of developing eight major weapons systems had increased from about \$47 billion in fiscal year 1998 to about \$72 billion by fiscal year 2003.<sup>8</sup> (GAO-03-98, January 2003)

---

<sup>7</sup> Congressional Budget Office, *The Long-Term Implications of Current Defense Plans: Detailed Update for Fiscal Year 2004* ([www.cbo.gov](http://www.cbo.gov), February 2004). Figures from this report are in constant fiscal year 2004 dollars.

<sup>8</sup> U.S. General Accounting Office, *Major Management Challenges and Program Risks: Department of Defense*, GAO-03-98 (Washington, D.C.: January 2003). Figures from this report are in constant fiscal year 2003 dollars.

These examples clearly demonstrate not only the severity of DOD's current problems, but also the importance of business systems modernization as a critical element in the department's transformation efforts to improve the economy, efficiency, and effectiveness of its operations, and to provide for transparency and accountability to Congress and American taxpayers.

## **Underlying Causes of Financial and Related Business Process Transformation Challenges**

Since May 1997,<sup>9</sup> we have highlighted in various testimonies and reports what we believe are the underlying causes of the department's inability to resolve its long-standing financial management and related business management weaknesses and fundamentally reform its business operations. We found that one or more of these causes were contributing factors to the financial management and related business process weaknesses we just described. Over the years, the department has undertaken many initiatives intended to transform its business operations departmentwide and improve the reliability of information for decision making and reporting but has not had much success because it has not addressed the following four underlying causes:

- a lack of sustained top-level leadership and management accountability for correcting problems;
- deeply embedded cultural resistance to change, including military service parochialism and stovepiped operations;
- a lack of results-oriented goals and performance measures and monitoring; and
- inadequate incentives and accountability mechanisms relating to business transformation efforts.

If not properly addressed, these root causes will likely result in the failure of current DOD initiatives.

---

<sup>9</sup>U.S. General Accounting Office, *DOD High-Risk Areas: Eliminating Underlying Causes Will Avoid Billions of Dollars in Waste*, GAO/T-NSIAD/AIMD-97-143 (Washington, D.C.: May 1, 1997).

## Lack of Sustained Leadership and Adequate Accountability

DOD has not routinely assigned accountability for performance to specific organizations or individuals who have sufficient authority to accomplish desired goals. For example, under the Chief Financial Officers Act of 1990,<sup>10</sup> it is the responsibility of the agency Chief Financial Officer (CFO) to establish the mission and vision for the agency's future financial management and to direct, manage, and provide oversight of financial management operations. However, at DOD, the Comptroller—who is by statute the department's CFO—has direct responsibility for only an estimated 20 percent of the data relied on to carry out the department's financial management operations. The other 80 percent comes from DOD's other business operations and is under the control and authority of other DOD officials.

In addition, DOD's past experience has suggested that top management has not had a proactive, consistent, and continuing role in integrating daily operations for achieving business transformation related performance goals. It is imperative that major improvement initiatives have the direct, active support and involvement of the Secretary and Deputy Secretary of Defense to ensure that daily activities throughout the department remain focused on achieving shared, agencywide outcomes and success. While the current DOD leadership, such as the Secretary, Deputy Secretary, and Comptroller, have certainly demonstrated their commitment to reforming the department, the magnitude and nature of day-to-day demands placed on these leaders following the events of September 11, 2001, clearly affect the level of oversight and involvement in business transformation efforts that these leaders can sustain. Given the importance of DOD's business transformation effort, it is imperative that it receive the sustained leadership needed to improve the economy, efficiency, and effectiveness of DOD's business operations. Based on our surveys of best practices of world-class organizations,<sup>11</sup> strong executive CFO and Chief Information Officer (CIO) leadership and centralized control over systems investments are essential to (1) making financial management an entitywide priority, (2)

---

<sup>10</sup> Chief Financial Officers Act of 1990, Pub. L. No. 101-576, 104 Stat. 2842, Nov. 15, 1990 (*codified, as amended in scattered sections of title 31, United States Code*).

<sup>11</sup> U.S. General Accounting Office, *Executive Guide: Creating Value Through World-class Financial Management*, GAO/AIMD-00-134 (Washington, D.C.: April 2000) and U.S. General Accounting Office, *Executive Guide: Maximizing the Success of Chief Information Officers: Learning From Leading Organizations*, GAO-01-376G (Washington, D.C.: February 2001).

providing meaningful information to decision makers, (3) building a team of people that delivers results, and (4) effectively leveraging technology to achieve stated goals and objectives.

### Cultural Resistance and Parochialism

Cultural resistance to change, military service parochialism, and stovepiped operations have all contributed significantly to the failure of previous attempts to implement broad-based management reforms at DOD. The department has acknowledged that it confronts decades-old problems deeply grounded in the bureaucratic history and operating practices of a complex, multifaceted organization. Recent audits reveal that DOD has made only small inroads in addressing these challenges. For example, the Bob Stump National Defense Authorization Act for Fiscal Year 2003<sup>12</sup> requires the DOD Comptroller to determine that each financial system improvement meets the specific conditions called for in the act before DOD obligates funds in amounts exceeding \$1 million. However, we found that most system improvement efforts involving obligations over \$1 million were not reviewed by the DOD Comptroller for the purpose of making that determination and that DOD continued to lack a mechanism for proactively identifying system improvement initiatives. We asked for, but DOD did not provide, comprehensive data for obligations in excess of \$1 million for business system modernization. Based on a comparison of the limited information available for fiscal years 2003 and 2004, we identified \$479 million in reported obligations by the military services that were not submitted to the DOD Comptroller for review.

In addition, in September 2003,<sup>13</sup> we reported that DOD continued to use a stovepiped approach to develop and fund its business system investments. Specifically, we found that DOD components receive and control funding for business systems investments without being subject to the scrutiny of the DOD Comptroller. DOD's ability to address its current "business-as-usual" approach to business system investments is further hampered by its lack of (1) a complete inventory of business systems (a condition we first highlighted in 1998), (2) a standard definition of what constitutes a business system, (3) a well-defined enterprise architecture, and (4) an

---

<sup>12</sup> Bob Stump National Defense Authorization Act for Fiscal Year 2003, Pub. L. No. 107-314, § 1004 (d), 116 Stat. 2458, 2629, Dec. 2, 2002.

<sup>13</sup> U.S. General Accounting Office, *DOD Business Systems Modernization: Important Progress Made to Develop*

effective approach for the control and accountability over business system investments. Until DOD develops and implements an effective strategy for overcoming resistance, parochialism, and stovepiped operations, its transformation efforts will not be successful.

### Lack of Results-Oriented Goals and Performance Measures

A key element of any major program is its ability to establish clearly defined goals and performance measures to monitor and report its progress to management. However, DOD has not yet established measurable, results-oriented goals to evaluate BMMP's cost, schedule and performance outcomes and results, or explicitly defined performance measures to evaluate the architecture quality, content, and utility of subsequent major updates to its initial business enterprise architecture (BEA). For example, in our September 2003 report<sup>14</sup>, we stated that DOD had not defined specific plans outlining how it intends to extend and evolve the initial BEA to include the missing scope and details that we identified. Instead, DOD's primary BEA goal was to complete as much of the architecture as it could within a set period of time. According to DOD, it intends to refine the initial BEA through at least six different major updates of its architecture between February 2004 and the second quarter of 2005. However, it remains unclear what these major updates will individually or collectively provide and how they contribute to achieving DOD's goals.

DOD recognizes that it needs to define measurable goals and performance measures. In its March 15, 2004, progress report to defense congressional committees on the status of BMMP's business transformation efforts, DOD reported that it plans to establish an initial approved program baseline to evaluate the cost, schedule, and performance of the BMMP. Given that DOD has reported disbursements of \$111 million since development efforts began in fiscal year 2002, it is critical that it establish meaningful, tangible, and measurable program goals and objectives—short-term and long-term.

Until DOD develops and implements clearly defined results-oriented goals for the overall program, including the architecture content of each major update of its architecture, the

---

*Business Enterprise Architecture, but Much Work Remains*, GAO-03-1018 (Washington, D.C.: September 19, 003).

department will continue to lack a clear measure of the BMMP's progress in transforming the department's business operations and in providing the Congress reasonable assurance that funds are being directed towards resolving the department's long-standing business operational problems.

### Lack of Incentives for Change

The final underlying cause of the department's long-standing inability to carry out needed fundamental reform has been the lack of incentives for making more than incremental change to existing "business-as-usual" operations, systems, and organizational structures. Traditionally, DOD has focused on justifying its need for more funding rather than on the outcomes its programs have produced. DOD has historically measured its performance by resource components such as the amount of money spent, people employed, or number of tasks completed. Incentives for its decision makers to implement changed behavior have been minimal or nonexistent.

The lack of incentive to change is evident in the business systems modernization area. Despite DOD's acknowledgement that many of its systems are error prone, duplicative, and stovepiped, DOD continues to allow its component organizations to make their own investments independently of one another and implement different system solutions to solve the same business problems. These stovepiped decision-making processes have contributed to the department's current complex, error-prone environment. The DOD Comptroller recently testified that DOD's actual systems inventory could be twice as many as the number of systems the department currently recognizes as its systems inventory. In March 2003, we reported that ineffective program management and oversight, as well as a lack of accountability, resulted in DOD continuing to invest hundreds of millions of dollars in system modernization efforts without any assurance that the projects will produce operational improvements commensurate with the amount invested.<sup>15</sup>

---

<sup>14</sup> GAO-03-1018

<sup>15</sup> GAO-03-465.



For example, the estimated cost of one of the business system investment projects that we reviewed increased by as much as \$274 million, while its schedule slipped by almost 4 years. After spending \$126 million, DOD terminated that project in December 2002, citing poor performance and increasing costs. GAO and the DOD IG have identified numerous business system modernization efforts that are not economically justified on the basis of cost, benefits and risk; take years longer than planned; and fall short of delivering planned or needed capabilities. Despite this track record, DOD continues to increase spending on business systems while at the same time it lacks the effective management and oversight needed to achieve real results. Without appropriate incentives to improve their project management, ongoing oversight, and adequate accountability mechanisms, DOD components will continue to develop duplicative and nonintegrated systems that are inconsistent with the Secretary's vision for reform.

To effect real change, actions are needed to (1) break down parochialism and reward behaviors that meet DOD-wide goals, (2) develop incentives that motivate decision makers to initiate and implement efforts that are consistent with better program outcomes, including saying "no" or pulling the plug early on a system or program that is failing, and (3) facilitate a congressional focus on results-oriented management, particularly with respect to resource allocation decisions.

## **Keys to Successful Reform**

As we have previously reported,<sup>16</sup> and the success of the more narrowly defined DOD initiatives we will discuss later illustrate, the following key elements collectively will enable the department to effectively address the underlying causes of its inability to resolve its long-standing financial and business management problems. These elements are

- addressing the department's financial management and related business operational challenges as part of a comprehensive, integrated, DOD-wide strategic plan for business reform;

---

<sup>16</sup> GAO-02-497T.

- providing for sustained and committed leadership by top management, including but not limited to the Secretary of Defense;
- establishing resource control over business systems investments;
- establishing clear lines of responsibility, authority, and accountability;
- incorporating results-oriented performance measures and monitoring progress tied to key financial and business transformation objectives;
- providing appropriate incentives or consequences for action or inaction;
- establishing an enterprise architecture to guide and direct business systems modernization investments; and
- ensuring effective oversight and monitoring.

These elements, which should not be viewed as independent actions but rather as a set of interrelated and interdependent actions, are reflected in the recommendations we have made to DOD and are consistent with those actions discussed in the department's April 2001 financial management transformation report.<sup>17</sup> The degree to which DOD incorporates them into its current reform efforts—both long and short term—will be a deciding factor in whether these efforts are successful. Thus far, the department's progress in implementing our recommendations has been slow.

## **DOD Business Transformation Efforts**

Over the years, we have given DOD credit for beginning numerous initiatives intended to improve its business operations. Unfortunately, most of these initiatives failed to achieve their intended objective in part, we believe, because they failed to incorporate key elements that in our experience are critical to successful reform. Today, we would like to discuss one very important broad-based initiative, the BMMP, DOD currently has underway that, if properly developed and implemented, will result in significant improvements in DOD's business operations. Within the next few months we intend to issue a report on the status of DOD's efforts to refine and implement its enterprise architecture and the results of our review of two on going

---

<sup>17</sup> Department of Defense, *Transforming Department of Defense Financial Management: A Strategy for Change* (Washington, D.C.: Apr. 13, 2001).

DOD system initiatives. In addition to the BMMP, DOD has undertaken several interim initiatives in recent years that have resulted in tangible, although limited, improvements. We believe that these tangible improvements were possible because DOD has accepted our recommendations and incorporated many of the key elements critical for reform. Furthermore, we would like to offer two suggestions for legislative consideration that we believe could significantly increase the likelihood of a successful business transformation effort at DOD.

### Business Management Modernization Program

The BMMP, which the department established in July 2001 following our recommendation that DOD develop and implement an enterprise architecture, is vital to the department's efforts to transform its business operations.<sup>18</sup> The purpose of the BMMP is to oversee development and implementation of a departmentwide BEA, transition plan, and related efforts to ensure that DOD business system investments are consistent with the architecture. A well-defined and properly implemented BEA can provide assurance that the department invests in integrated enterprisewide business solutions and, conversely, can help move resources away from nonintegrated business system development efforts. As we reported in July 2003,<sup>19</sup> DOD had developed an initial version of its departmentwide architecture for modernizing its current financial and business operations and systems and had expended tremendous effort and resources in doing so. However, substantial work remains before the architecture will be sufficiently detailed and the means for implementing it will be adequately established to begin to have a tangible impact on improving DOD's overall business operations. We cannot overemphasize the degree of difficulty DOD faces in developing and implementing a well-defined architecture to provide the foundation that will guide its overall business transformation effort.

On the positive side, during its initial efforts to develop the architecture, the department established some of the architecture management capabilities advocated by best practices and federal guidance,<sup>20</sup> such as establishing a program office, designating a chief architect, and using

---

<sup>18</sup> GAO-01-525.

<sup>19</sup> GAO-03-877R.

<sup>20</sup> U.S. General Accounting Office, *Information Technology: A Framework for Assessing and Improving Enterprise Architecture Management (Version 1.1)*, GAO-03-584G (Washington, D.C.: April 2003).

an architecture development methodology and automated tool. Further, DOD's initial version of its business enterprise architecture provided a foundation on which to build and ultimately produce a well-defined business enterprise architecture. For example, in September 2003,<sup>21</sup> we reported that the "To Be" descriptions address, to at least some degree, how DOD intends to operate in the future, what information will be needed to support these future operations, and what technology standards should govern the design of future systems.

While some progress has been made, DOD has not yet taken important steps that are critical to its ability to successfully use the enterprise architecture to drive reform throughout the department's overall business operations. For example, DOD has not yet defined and implemented the following.

- Detailed plans to extend and evolve its initial architecture to include the missing scope and detail required by the Bob Stump National Defense Authorization Act for Fiscal Year 2003 and other relevant architectural requirements. Specifically, (1) the initial version of the BEA excluded some relevant external requirements, such as requirements for recording revenue, and lacked or provided little descriptive content pertaining to its "As Is" and "To Be" environments and (2) DOD had not yet developed the transition plan needed to provide a temporal road map for moving from the "As Is" to the "To Be" environment.
- An effective approach to select and control business system investments<sup>22</sup> for obligations exceeding \$1 million. As we previously stated, and it bears repeating here, DOD components currently receive direct funding for their business systems and continue to make their own parochial decisions regarding those investments without having received the scrutiny of the DOD Comptroller as required by the Bob Stump National Defense Authorization Act for Fiscal Year of 2003. Later, we will

---

<sup>21</sup> GAO-03-1018.

<sup>22</sup> Business systems include financial and nonfinancial systems, such as civilian personnel, finance, health, logistics, military personnel, procurement, and transportation, with the common element being the generation or use of financial data to support DOD's business operations.

offer a suggestion for improving the management and oversight of the billions of dollars DOD invests annually in business systems.

DOD invests billions of dollars annually to operate, maintain, and modernize its business systems. For fiscal year 2004, the department requested approximately \$28 billion in IT funding to support a wide range of military operations as well as DOD business systems operations, of which approximately \$18.8 billion<sup>23</sup>—\$5.8 billion for business systems and \$13 billion for business systems infrastructure—relates to the operation, maintenance, and modernization of the department's reported thousands of business systems. The \$18.8 billion is spread across the military services and defense agencies, with each receiving its own funding for IT investments.

However, as we reported,<sup>24</sup> DOD lacked an efficient and effective process for managing, developing, and implementing its business systems. These long-standing problems continue despite the significant investments in business systems by DOD components each year. For example, in March 2003 we reported that DOD's oversight of four DFAS projects we reviewed had been ineffective.<sup>25</sup> Investment management responsibility for the four projects rested with the Defense Finance and Accounting Service (DFAS), the DOD Comptroller, and the DOD CIO. In discharging this responsibility, each had allowed project investments to continue year after year, even through the projects had been marked by cost increases, schedule slippages, and capability changes. As a result DOD had invested approximately \$316 million in four DFAS system modernization projects without demonstrating that this substantial investment would markedly improve DOD financial management information for decision making and financial reporting purposes.

Specifically, we found that four DFAS projects reviewed lacked an approved economic analysis that reflected the fact that expected project costs had increased, while in some cases the benefits had decreased. For instance as we previously stated, the estimated cost of one project—referred to as the Defense Procurement Payment System (DPPS)—had increased by as much as \$274

---

<sup>23</sup>The remaining \$9 billion is for National Security Systems. These systems are intelligence systems, cryptologic activities related to national security, military command and control systems, and equipment that is an integral part of a weapon or weapons system or is critical to the direct fulfillment of military or intelligence mission.

<sup>24</sup> GAO-03-465 and GAO-03-553T.

<sup>25</sup> GAO-03-465.

million, while its schedule slipped by almost 4 years. Such project analyses provide the requisite justification for decision makers to use in determining whether to invest additional resources in anticipation of receiving commensurate benefits and mission value. For each of the four projects we reviewed we found that DOD oversight entities—DFAS, the DOD Comptroller, and the DOD CIO—did not question the impact of the cost increases and schedule delays, and allowed the projects to proceed in the absence of the requisite analytical justification. Furthermore, in one case, they allowed a project estimated to cost \$270 million, referred to as the DFAS Corporate Database/DFAS Corporate Warehouse (DCD/DCW), to proceed without an economic analysis. In another case, they allowed DPPS to continue despite known concerns about the validity of the project’s economic analysis.

DOD subsequently terminated two—DPPS and the Defense Standard Disbursing System (DSDS)—of the four DFAS system modernization projects reviewed. As we previously mentioned, DPPS was terminated due to poor program performance and increasing costs after 7 years of effort and an investment of over \$126 million. DFAS terminated DSDS after approximately 7 years of effort and an investment of about \$53 million, noting that a valid business case for continuing the effort could not be made. These two terminated projects were planned to provide DOD the capability to address some of DOD’s long-standing contract and vendor payment problems.

In addition to project management issues that continue to result in systems that do not perform as expected and cost more than planned, we found that DOD continues to lack a complete and reliable inventory of its current systems. In September 2003, we reported that DOD had created a repository of information about its existing systems inventory of approximately 2,300 business systems (up from 1,731 in October 2002) as part of its ongoing business systems modernization program, and consistent with our past recommendation.<sup>26</sup> Due to its lack of visibility over systems departmentwide, DOD had to rely upon data calls to obtain its information. Unfortunately, due to its lack of an effective methodology and process for identifying business systems, including a clear definition of what constitutes a business system, DOD continues to lack assurance that its systems inventory is reliable and complete. In fact, the DOD Comptroller

---

<sup>26</sup> U.S. General Accounting Office, *Financial Management: DOD Improvement Plan Needs Strategic Focus*, GAO-

testified last week before the Senate Armed Services Subcommittee on Readiness and Management Support that the size of DOD’s actual systems inventory could be twice the size currently reported. This lack of visibility over current business systems in use throughout the department hinders DOD’s ability to identify and eliminate duplicate and nonintegrated systems and transition to its planned systems environment in an efficient and effective manner.

Of the 2,274 business systems recorded in DOD’s systems inventory repository, the department reportedly has 665 systems to support human resource management, 565 systems to support logistical functions, 542 systems to perform finance and accounting functions, and 210 systems to support strategic planning and budget formulation. Table 1, which presents the composition of DOD business systems by functional area, reveals the numerous and redundant systems operating in the department today.

**Table 1: Reported DOD Business Systems by Domain and Functional Area**

<u>Domain</u>	<b>Air Force</b>	<b>Army</b>	<b>Navy/ Marine Corps</b>	<b>DFAS</b>	<b>Other</b>	<b>Total</b>
Acquisition	27	31	61	3	21	143
Accounting and finance	43	88	195	165	51	542
Human resource management	71	387	86	33	88	665
Installations and environment	12	98	9	1	8	128
Logistics	180	191	104	11	79	565
Strategic planning and budgeting	23	63	98	15	11	210
Enterprise information environment	1	5	2	3	10	21
<b>Total</b>	<b>357</b>	<b>863</b>	<b>555</b>	<b>231</b>	<b>268</b>	<b>2,274</b>

Source: GAO analysis of BMMP data.

As we have previously reported,<sup>27</sup> these numerous systems have evolved into the overly complex and error-prone operation that exists today, including (1) little standardization across DOD components, (2) multiple systems performing the same tasks, (3) the same data stored in multiple systems, (4) manual data entry into multiple systems, and (5) a large number of data translations and interfaces that combine to exacerbate problems with data integrity. The department has recognized the uncontrolled proliferation of systems and the need to eliminate as many systems as possible and integrate and standardize those that remain. In fact, the two terminated DFAS

01-764 (Washington, D.C.: Aug. 17, 2001).

<sup>27</sup> U.S. General Accounting Office, *DOD Financial Management: Important Steps Underway But Reform Will*

projects were intended to reduce the number of systems or eliminate a portion of different systems that perform the same function. For example, DPPS was intended to consolidate eight contract and vendor pay systems and DSDS was intended to eliminate four different disbursing systems.

Until DOD completes its efforts to refine and implement its enterprise architecture and transition plan, and develop and implement an effective approach for selecting and controlling business system investments, DOD will continue to lack (1) a comprehensive and integrated strategy to guide its business process and system changes, and (2) results-oriented measures to monitor and measure progress, including whether system development and modernization investment projects adequately incorporate leading practices used by the private sector and federal requirements and achieve performance and efficiency commensurate with the cost. These elements are critical to the success of DOD's BMMP.

Developing and implementing a BEA for an organization as large and complex as DOD is a formidable challenge, but it is critical to effecting the change required to achieve the Secretary's vision of relevant, reliable, and timely financial and other management information to support the department's vast operations. As mandated, we plan to continue to report on DOD's progress in developing the next version of its architecture, developing its transition plan, validating its "As Is" systems inventory, and controlling its system investments.

### Interim Initiatives

Since DOD's overall business process transformation is a long-term effort, in the interim it is important for the department to focus on improvements that can be made using, or requiring only minor changes to, existing automated systems and processes. As demonstrated by the examples we will highlight in this testimony, leadership, real incentives, accountability, and oversight and monitoring—key elements to successful reform—have brought about improvements in some DOD operations, such as more timely commercial payments, reduced payment recording errors, and significant reductions in individually billed travel card delinquency rates.

---

*Require a Long-term Commitment*, GAO-02-784T (Washington, D.C.: June 4, 2002).



To help achieve the department's goal of improved financial information, the DOD Comptroller has developed a Financial Management Balanced Scorecard that is intended to align the financial community's strategy, goals, objectives, and related performance measures with the departmentwide risk management framework established as part of DOD's Quadrennial Defense Review, and with the President's Management Agenda. To effectively implement the balanced scorecard, the Comptroller is planning to cascade the performance measures down to the military services and defense agency financial communities, along with certain specific reporting requirements. DOD has also developed a Web site where implementation information and monthly indicator updates will be made available for the financial communities' review. At the departmentwide level, certain financial metrics will be selected, consolidated, and reported to the top levels of DOD management for evaluation and comparison. These "dashboard" metrics are intended to provide key decision makers, including Congress, with critical performance information at a glance, in a consistent and easily understandable format.

DFAS has been reporting the metrics cited below for several years, which, under the leadership of DFAS' Director and DOD's Comptroller, have reported improvements, including the following.

- From April 2001 to January 2004, DOD reduced its commercial pay backlogs (payment delinquencies) by 55 percent.
- From March 2001 to December 2003, DOD reduced its payment recording errors by 33 percent.
- The delinquency rate for individually billed travel cards dropped from 18.4 percent in January 2001 to 10.7 percent in January 2004.

Using DFAS' metrics, management can quickly see when and where problems are arising and can focus additional attention on those areas. While these metrics show significant improvements from 2001 to today, statistics for the last few months show that progress has slowed or even

taken a few steps backward for payment recording errors and commercial pay backlogs. Our report last year on DOD's metrics program<sup>28</sup> included a caution that, without modern integrated systems and the streamlined processes they engender, reported progress may not be sustainable if workload is increased.

Since we reported problems with DOD's purchase card program, DOD and the military services have taken actions to address all of our 109 recommendations. In addition, we found that DOD and the military services took action to improve the purchase card program consistent with the requirements of the Bob Stump National Defense Authorization Act for Fiscal Year 2003 and the DOD Appropriations Act for Fiscal Year 2003.<sup>29</sup> Specifically, we found that DOD and the military services had done the following.

- Substantially reduced the number of purchase cards issued. According to GSA records, DOD had reduced the total number of purchase cards from about 239,000 in March 2001 to about 134,609 in January 2004. These reductions have the potential to significantly improve the management of this program.
- Issued policy guidance to field activities to (1) perform periodic reviews of all purchase card accounts to reestablish a continuing bona fide need for each card account, (2) cancel accounts that were no longer needed, and (3) devise additional controls over infrequently used accounts to protect the government from potential cardholder or outside fraudulent use.
- Issued disciplinary guidelines, separately, for civilian and military employees who engage in improper, fraudulent, abusive, or negligent use of a government charge card.

---

<sup>28</sup> U.S. General Accounting Office, *Financial Management: DOD's Metrics Program Provides Focus for Improving Performance*, GAO-03-457, (Washington, D.C.: Mar. 28, 2003).

<sup>29</sup> The Department of Defense Appropriations Act for Fiscal Year 2003, Pub. L. No. 107-248, § 8149, 116 Stat. 1519, 1572, Oct. 23, 2002.

In addition, to monitor the purchase card program, the DOD IG and the Navy have prototyped and are now expanding a data-mining capability to screen for and identify high-risk transactions (such as potentially fraudulent, improper, and abusive use of purchase cards) for subsequent investigation. On June 27, 2003, the DOD IG issued a report<sup>30</sup> summarizing the results of an in-depth review of purchase card transactions made by 1,357 purchase cardholders. The report identified 182 cardholders who potentially used their purchase cards inappropriately or fraudulently.

We believe that consistent oversight played a major role in bringing about these improvements in DOD's purchase and travel card programs. During 2001, 2002, and 2003, seven separate congressional hearings were held on the Army and Navy purchase and individually billed travel card programs. Numerous legislative initiatives aimed at improving DOD's management and oversight of these programs also had a positive impact.

Another important initiative underway at the department pertains to financial reporting. Under the leadership of DOD Comptroller, the department is working to instill discipline into its financial reporting processes to improve the reliability of the department's financial data. Resolution of serious financial management and related business management weaknesses is essential to achieving any opinion on the DOD consolidated financial statements. Pursuant to the requirements in section 1008 of the National Defense Authorization Act for Fiscal Year 2002,<sup>31</sup> DOD has reported for the past 3 years on the reliability of the department's financial statements, concluding that the department is not able to provide adequate evidence supporting material amounts in its financial statements. Specifically, DOD stated that it was unable to comply with applicable financial reporting requirements for (1) property, plant, and equipment, (2) inventory and operating materials and supplies, (3) environmental liabilities, (4) intragovernmental eliminations and related accounting entries, (5) disbursement activity, and (6) cost accounting by responsibility segment. Although DOD represented that the military retirement health care liability data had improved for fiscal year 2003, the cost of direct health care provided by DOD-managed military treatment facilities was a significant amount of DOD's total recorded health

---

<sup>30</sup> Department of Defense, Office of the Inspector General, *Summary Report on Joint Review of Selected DOD Purchase Card Transactions*, D2003-109 (Washington, D.C.: June 27, 2003).

<sup>31</sup> National Defense Authorization Act for Fiscal Year 2003, Pub. L. No. 107-107, §1008, 115 Stat. 1012, 1204, Dec.

care liability and was based on estimates for which adequate support was not available. DOD has indicated that by acknowledging its inability to produce reliable financial statements, as required by the act, the department saves approximately \$23 million a year through reduction in the level of resources needed to prepare and audit financial statements. However, DOD has set the goal of obtaining a favorable opinion on its fiscal year 2007 departmentwide financial statements. To this end, DOD components and agencies have been tasked with addressing material line item deficiencies in conjunction with the BMMP. This is an ambitious goal and we have been requested by Congress to review the feasibility and cost effectiveness of DOD's plans for obtaining such an opinion within the stated time frame.

To instill discipline in its financial reporting process, the DOD Comptroller requires DOD's major components to prepare quarterly financial statements along with extensive footnotes that explain any improper balances or significant variances from previous year quarterly statements. All of the statements and footnotes are analyzed by Comptroller office staff and reviewed by the Comptroller. In addition, the midyear and end-of-year financial statements must be briefed to the DOD Comptroller by the military service Assistant Secretary for Financial Management or the head of the defense agency. We have observed several of these briefings and have noted that the practice of preparing and explaining interim financial statements has led to the discovery and correction of numerous recording and reporting errors.

If DOD continues to provide for active leadership, along with appropriate incentives and accountability mechanisms, improvements will continue to occur in its programs and initiatives.

#### Suggestions for Legislative Consideration

We would like to offer two suggestions for legislative consideration that we believe could contribute significantly to the department's ability to not only address the impediments to DOD success but also to incorporate needed key elements to successful reform. These suggestions would include the creation of a chief management official and the centralization of responsibility

and authority for business system investment decisions with the domain<sup>32</sup> leaders responsible for the department's various business areas, such as logistics and human resource management.

### Chief Management Official

Previous failed attempts to improve DOD's business operations illustrate the need for sustained involvement of DOD leadership in helping to assure that the DOD's financial and overall business process transformation efforts remain a priority. While the Secretary and other key DOD leaders have certainly demonstrated their commitment to the current business transformation efforts, the long-term nature of these efforts requires the development of an executive position capable of providing strong and sustained executive leadership over a number of years and various administrations. The day-to-day demands placed on the Secretary, the Deputy Secretary, and others make it difficult for these leaders to maintain the oversight, focus, and momentum needed to resolve the weaknesses in DOD's overall business operations. This is particularly evident given the demands that the Iraq and Afghanistan postwar reconstruction activities and the continuing war on terrorism have placed on current leaders. Likewise, the breadth and complexity of the problems preclude the Under Secretaries, such as the DOD Comptroller, from asserting the necessary authority over selected players and business areas.

While sound strategic planning is the foundation upon which to build, sustained leadership is needed to maintain the continuity needed for success. One way to ensure sustained leadership over DOD's business transformation efforts would be to create a full-time executive level II position for a chief management official who would serve as the Principal Under Secretary of Defense for Management.<sup>33</sup> This position would provide the sustained attention essential for addressing key stewardship responsibilities such as strategic planning, performance and financial management, and business systems modernization in an integrated manner, while also facilitating the overall business transformation operations within DOD. This position could be

---

<sup>32</sup>DOD has one Enterprise Information Environment Mission, and six departmental domains including (1) acquisition/ procurement, (2) finance, accounting, and financial management, (3) human resource management, (4) logistics, (5) strategic planning and budgeting, and (6) installations and environment.

<sup>33</sup> On September 9, 2002, GAO convened a roundtable of executive branch leaders and management experts to discuss the Chief Operating Officer concept. For more information see U.S. General Accounting Office, *Highlights of a GAO Roundtable: The Chief Operating Officer Concept: A Potential Strategy to Address Federal Governance Challenges*, GAO-03-192SP (Washington, D.C.: Oct. 4, 2002).

filled by an individual, appointed by the President and confirmed by the Senate, for a set term of 7 years with the potential for reappointment. Such an individual should have a proven track record as a business process change agent in large, complex, and diverse organizations—experience necessary to spearhead business process transformation across the department, and potentially administrations, and serve as an integrator for the needed business transformation efforts. In addition, this individual would enter into an annual performance agreement with the Secretary that sets forth measurable individual goals linked to overall organizational goals in connection with the department’s overall business transformation efforts. Measurable progress towards achieving agreed upon goals would be a basis for determining the level of compensation earned, including any related bonus. In addition, this individual’s achievements and compensation would be reported to Congress each year.

#### Central Control Over System Investments

We have made numerous recommendations to DOD intended to improve the management oversight and control of its business systems investments. However, as previously mentioned, progress in achieving this control has been slow and, as a result, DOD has little or no assurance that current business systems investments are being spent in an economically efficient and effective manner. DOD’s current systems funding process has contributed to the evolution of an overly complex and error-prone information technology environment containing duplicative, nonintegrated, and stovepiped systems. Given that DOD plans to spend approximately \$19 billion on business systems and related infrastructure for fiscal year 2004—including an estimated \$5 billion in modernization money—it is critical that actions be taken to gain more effective control over such business systems funding.

The second suggestion we have for legislative action to address this issue, consistent with our open recommendations to DOD, is to establish specific management oversight, accountability, and control of funding with the “owners” of the various functional areas or domains. This legislation would define the scope of the various business areas (e.g., acquisition, logistics, finance and accounting) and establish functional responsibility for management of the portfolio of business systems in that area with the relevant Under Secretary of Defense for the six

departmental domains and the CIO for the Enterprise Information Environment Mission (information technology infrastructure). For example, planning, development, acquisition, and oversight of DOD's portfolio of logistics business systems would be vested in the Under Secretary of Defense for Acquisition, Technology, and Logistics.

We believe it is critical that funds for DOD business systems be appropriated to the domain owners in order to provide for accountability, transparency, and the ability to prevent the continued parochial approach to systems investment that exists today. The domains would establish a hierarchy of investment review boards with DOD-wide representation, including the military services and Defense agencies. These boards would be responsible for reviewing and approving investments to develop, operate, maintain, and modernize business systems for the domain portfolio, including ensuring that investments were consistent with DOD's BEA. All domain owners would be responsible for coordinating their business systems investments with the chief management official who would chair the Defense Business Systems Modernization Executive Committee and provide a cross-domain perspective. Domain leaders would also be required to report to Congress through the chief management official and the Secretary of Defense on applicable business systems that are not compliant with review requirements and to include a summary justification for noncompliance.

## **Conclusion**

As seen again in Iraq, the excellence of our military forces is unparalleled. However, that excellence is often achieved in the face of enormous challenges in DOD's financial management and other business areas, which have serious and far-reaching implications related to the department's operations and critical national defense mission. Our recent work has shown that DOD's long-standing financial management and business problems have resulted in fundamental operational problems, such as failure to properly pay mobilized Army Guard soldiers and the inability to provide adequate accountability and control over supplies and equipment shipments in support of Operation Iraqi Freedom. Further, the lack of adequate transparency and appropriate accountability across all business areas has resulted in certain fraud, waste, and abuse and hinders DOD's attempts to develop world-class operations and activities to support its

forces. As our nation continues to be challenged with growing budget deficits and increasing pressure to reduce spending levels, every dollar that DOD can save through improved economy and efficiency of its operations is important.

DOD's senior leaders have demonstrated a commitment to transforming the department and improving its business operations and have taken positive steps to begin this effort. We believe that implementation of our open recommendations and our suggested legislative initiatives would greatly improve the likelihood of meaningful, broad-based reform at DOD. The continued involvement and monitoring by congressional committees will also be critical to ensure that DOD's initial transformation actions are sustained and extended and that the department achieves its goal of securing the best performance and highest measure of accountability for the American people. We commend the Subcommittee for holding this hearing and we encourage you to use this vehicle, on at least an annual basis, as a catalyst for long overdue business transformation at DOD.

Mr. Chairman, this concludes our statement. We would be pleased to answer any questions you or other members of the Subcommittee may have at this time.

## **Contacts and Acknowledgments**

For further information about this testimony, please contact Gregory D. Kutz at (202) 512-9095 or [kutzg@gao.gov](mailto:kutzg@gao.gov), Randolph Hite at (202) 512-3439 or [hiter@gao.gov](mailto:hiter@gao.gov), or Evelyn Logue at 202-512-3881. Other key contributors to this testimony include Bea Alff, Meg Best, Molly Boyle, Art Brouk, Cherry Clipper, Mary Ellen Chervenik, Francine Delvecchio, Abe Dymond, Eric Essig, Gayle Fischer, Geoff Frank, John Kelly, Patricia Lentini, Elizabeth Mead, Mai Nguyen, Greg Pugnetti, Cary Russell, John Ryan, Darby Smith, Carolyn Voltz, Marilyn Wasleski, and Jenniffer Wilson.

(192127)