



Department of Defense Agency Financial Report



2010

Addendum A
November 15, 2010

ADDENDUM A – OTHER ACCOMPANYING INFORMATION

Other Accompanying Information provides additional details that support the fiscal year (FY) 2010 Department of Defense (DoD) Agency Financial Report (AFR). This addendum includes the following sections:

- Inspector General’s (IG) summary of the most significant management and performance challenges facing the Department, to include DoD’s responses to the IG’s assessments.
- Managers’ Internal Control Program and Financial Statement Audit Material Weaknesses.
- Improper Payments Information Act Reporting.

MANAGEMENT AND PERFORMANCE CHALLENGES

The Reports Consolidation Act of 2000 requires that the AFR include a statement prepared by the Agency’s Inspector General that summarizes what he or she considers to be the most serious management and performance challenges facing the Agency and a brief assessment of the progress made in addressing those challenges. The DoD IG identified the following eight management and performance challenges facing the Department in FY 2010:

1. Financial Management
2. Acquisition Processes and Contract Management
3. Joint Warfighting and Readiness
4. Information Assurance, Security, and Privacy
5. Health Care
6. Equipping and Training Iraq and Afghan Security Forces
7. Nuclear Enterprise
8. American Recovery and Reinvestment Act

The following tables outline these challenges and include both the IG’s and the Department’s management assessment of progress made in addressing these issues.

1. Financial Management	
1-1A. Financial Information	IG Summary of Challenge
<p>The Department continues to face financial management challenges that adversely affect its ability to provide reliable, timely, and useful financial and managerial data needed to support operating, budgeting, and policy decisions. Since the 1990s, the DoD IG has identified financial management as a management challenge. The DoD’s financial management problems are so significant that they constitute the single largest and most challenging impediment to the U.S. Government’s ability to obtain an opinion on its consolidated financial statements.</p> <p>In the FY 2009 audit opinion on DoD’s consolidated financial statements, the DoD IG reported the same 13 material internal control weaknesses as the previous year. These pervasive and longstanding financial management issues directly affect DoD’s ability to obtain an unqualified opinion on its financial statements. These weaknesses affect the safeguarding of assets, proper use of funds, and impair the prevention and identification of fraud, waste, and abuse.</p>	

Department of Defense Agency Financial Report for FY 2010

1-1B. Financial Information	IG Assessment of Progress
<p>A significant measure of DoD's ongoing progress in the area of financial management is the ability to obtain an unqualified opinion on its financial statements. The Defense Commissary Agency, Defense Contract Audit Agency, Defense Finance and Accounting Service, Military Retirement Fund, National Reconnaissance Office, U.S. Army Corps of Engineers, and DoD IG financial statements all have received unqualified audit opinions.</p> <p>One of DoD's goals is to improve its ability to provide timely, complete, and accurate financial information through an integrated set of enterprise business systems. The Department, through the Enterprise Transition Plan, plans to support metrics in improved financial information.</p> <p>In addition, the IG is auditing the U.S. Marine Corps' (USMC) Statement of Budgetary Resources, the first Military Component to undergo such an audit. While the opinion has not yet been determined and the USMC has encountered many challenges during this first-time audit, the Department is learning from this audit experience.</p>	
1-2A. Improving Financial Information	IG Summary of Challenge
<p>The following elements and actions continue to be key for improving DoD's financial management:</p> <ul style="list-style-type: none"> • Create an environment that effectively identifies, coordinates, implements, and monitors financial management improvement efforts and holds managers accountable for the successful and timely implementation of these efforts. • Fully implement and maintain an effective internal review and monitoring process to identify all material financial management and reporting deficiencies, internal control weaknesses, and quality of data issues. • Develop corrective action plans that adequately correct deficiencies and result in financial reporting that is in accordance with accounting principles generally accepted in the United States (USGAAP). • Implement corrective action plans that address systems, controls, reporting, and quality of data. 	
1-2B. Improving Financial Information	IG Assessment of Progress
<p>The DoD's ongoing initiatives in financial management improvement demonstrate that management is responding to the significant and pervasive financial management issues identified. The Department is positioning itself to leverage planned systems and business improvements to achieve sustainable, long-term solutions.</p> <p>Public Law 111-84, "National Defense Appropriations Act for Fiscal Year 2010," Section 1003, October 28, 2009, requires that the Department assert to audit readiness no later than September 30, 2017. This requires the Financial Improvement and Audit Readiness (FIAR) Plan correct the financial management deficiencies that impair DoD's ability to prepare timely, reliable, and complete financial management information and ensure financial statements are ready for audit. The priorities set forth in Section 1003 include improving budgetary information to achieve an unqualified opinion on DoD's Statement of Budgetary Resources and, as a secondary goal, improving the accuracy and reliability of management information of mission-critical assets and validating its accuracy through existence and completeness audits.</p> <p>The Department adjusted its FIAR plan to align with the requirements outlined in Public Law 111-84. The May 2010 plan updates and refines FIAR priorities to focus on improving controls and processes that support the information used most often to manage the Department and to continue working toward financial, information technology and supporting documentation improvements that facilitate achievement of unqualified audit opinions on financial statements. The new strategy consists of five waves of priority:</p> <ul style="list-style-type: none"> • Wave 1—Appropriations received audit; • Wave 2—Statement of Budgetary Resources audit; • Wave 3—Mission-critical asset existence and completeness audit; • Wave 4—Full audit, except for legacy asset valuation; and • Wave 5—Full financial statement audit. <p>In response to Public Law 110-181, "National Defense Authorization Act for Fiscal Year 2008," Section 904, January 28, 2008, the Department established the DoD Chief Management Officer (CMO) and the Military Department CMO positions, which are responsible for the management and effective and efficient organization of the business operations of the Department or the respective Military Department.</p>	

Additionally, Section 908, "Business Transformation Initiatives for the Military Departments," Public Law 110-417, "Duncan Hunter National Defense Authorization Act for Fiscal Year 2009," October 14, 2008, assigns responsibilities and establishes an organizational structure within each Military Department for business transformation.

The IG considers the following DoD financial management efforts to be limited successes:

- Implementation of integrated organizational structures and processes to address financial management improvement;
- Assignment of accountability to DoD managers; and
- DoD improvement initiatives at the entity and line item level.

Although the IG anticipates that the Department will need to make improvements in these areas, the IG considers these to be critical steps for establishing a culture and institutionalizing a structure that will facilitate identifying internal control weaknesses and planning effectively for their resolution. This culture and structure also will hold DoD managers accountable for improving internal controls over financial reporting. Further, these steps should result in a financial management structure that can provide accurate, relevant, and timely financial management information for decision-making.

1. Financial Management

Management's Overall Assessment

The Department updated its financial improvement and audit readiness strategy to focus on improving the processes, controls, and systems that support the information most often needed to manage the Department, while continuing to work toward financial improvements that will result in receipt of an unqualified audit opinion on the financial statements. Components have developed consistent, detailed Financial Improvement Plans to accomplish the new priorities. To achieve these objectives, the USD(C) assigned a high priority to:

- Budgetary Information. Recognizing that many decisions are budget related (e.g., status of funds received, obligated, and expended), DoD's priorities focus on improving the processes, controls, and systems that produce budgetary information that is timely and accurate. This focus will allow the Department to improve information most often used by management and meet the goal of obtaining auditable financial statements, beginning first with the Statement of Budgetary Resources (SBR).
- Mission-Critical Asset Information. This second priority focuses on improving the information needed to effectively manage DoD's mission-critical assets. Mission-critical assets include Military Equipment, Real Property, Inventory, Operating Materials and Supplies, and General Equipment. Achieving this objective not only will ensure reliable information for managing DoD assets, but is an essential first step to reporting the value of these assets on DoD's Balance Sheet.

To date, the Department has made measured progress in improving financial information. Specifically, the U.S. Marine Corps (USMC)'s Statement of Budgetary Resources financial statement is under audit, which has resulted in significant improvements to budget and other financial information. In addition, the Defense Information Systems Agency (DISA) Working Capital Fund remediated financial management deficiencies and asserted audit readiness for its financial statements. The Air Force and Defense Logistics Agency (DLA) asserted audit readiness on appropriations received in the fourth quarter, FY 2010.

The Department will continue to implement Enterprise Resource Planning (ERP) solutions and modernize other business and financial systems, which enable the use of standard business processes and controls across the Department and will improve the financial information that feeds the preparation of the financial statements. The ERP initiatives must comply with the Standardized Financial Information Structure, which also will assist the Department in complying with the Federal Financial Management Improvement Act (FFMIA) and Business Enterprise Architecture (BEA) requirements. The Investment Review Boards (IRBs) and the Defense Business System Management Committee will continue oversight of ERP system implementation to ensure progress continues and implementation issues are effectively resolved in a timely manner.

To enhance financial improvement and audit readiness oversight and governance, the USD(C) created the FIAR Governance Board, which is co-chaired by the USD(C) and Deputy CMO, and includes Military Department CMOs as well as DoD's financial management senior leaders and senior representatives from the functional communities. The Component CMOs facilitate prioritization of financial management improvement efforts across the functional areas of the Department and are critical to DoD's success. The Department also established a DoD Audit Advisory Committee (DAAC), which provides independent advice to the Secretary of Defense regarding DOD's financial management, including financial reporting policies, processes, systems of internal controls, audit

processes, and processes for monitoring compliance with relevant laws and regulations. The Committee members, appointed by the Secretary of Defense to three-year terms, are distinguished members of the audit, accounting, and financial communities.

In summary, the Department agrees with the IG's summary of challenges and assessment of progress and continues to work aggressively to resolve the long-standing material weaknesses and achieve auditable financial statements.

2. Acquisition Processes and Contract Management

2-1A. Acquisition Workforce

IG Summary of Challenge

Since the 1990s, DoD IG has identified DoD acquisition and contract management processes as a challenge area. Acquisition initiatives that began in the 1990s led to reductions in acquisition oversight assets. When the spending trend dramatically reversed after September 11, 2001, the Department was not able to react quickly to the need for more contract and oversight support. The emphasis on urgency to support the war effort, especially for contracting in an expeditionary environment, has only served to increase the challenges. In FY 2010, the Defense budget--including funding for contingency operations--could exceed \$700 billion. This total is more than double the amount in the DoD budget that preceded September 11, 2001. Keeping pace with this spending would be a difficult proposition even if acquisition and oversight assets were increasing at a proportional rate; however, as of 2009, the level of staffing of the acquisition workforce was below those in 1998.

2-1B. Acquisition Workforce

IG Assessment of Progress

Efforts to train and ready the DoD acquisition workforce to handle a significant increase in acquisition workload demand and the complexity resulting from extensive services contracting, counterinsurgency operations, and other critical missions, continues to challenge the Department. As noted in the February 2010 Quadrennial Defense Review, the Department recognizes the need to continue to: develop a total defense workforce to better support the urgent needs of the warfighter; buy weapons that are usable, affordable, and truly needed; and ensure that taxpayer dollars are spent wisely and responsibly. In addition, the Defense Acquisition Strategic Workforce Plan, dated April 2010, captures how the Department will support the intent of the President and the Secretary of Defense to improve the acquisition workforce. The report highlights the theme of the Under Secretary of Defense for Acquisition, Technology, and Logistics, which serves as a reminder that while "workforce size is important, quality is paramount."

Numerous initiatives, both from within and resulting from proposed legislation, continue to address acquisition workforce challenges. Specifically, on April 6, 2009, the Secretary of Defense announced his intent to reform the DoD acquisition process by increasing the size of the Defense Acquisition Workforce (DAW) by 20,000 employees. The DoD's initiatives appear on track, with the acquisition workforce growing from approximately 126,000 to 133,000 personnel in FY 2009. The Department will continue its efforts to return the acquisition workforce to a level above the 146,000 personnel in 1998.

Further, in April 2010, the House of Representatives passed a new acquisition reform bill, H.R. 5013, "Implementing Management for Performance and Related Reforms to Obtain Value in Every Acquisition Act of 2010" (the IMPROVE Acquisition Act). This bill would require the Department to better manage the defense acquisition system; incentivize the development of a larger, better trained, and more professional acquisition workforce; reform DoD's financial management with a view toward ensuring greater auditability of the DoD Components' financial statements; and seek to expand the defense industrial base to enhance competition.

2-2A. Major Weapon Acquisition

IG Summary of Challenge

The Department continues to be challenged in its ability to execute acquisition programs without significant cost overruns and major schedule delays. The DoD acquisition mission represents the largest buying enterprise in the world. The number of Major Defense Acquisition Programs (MDAPs) increased to 103 in FY 2009, with little corresponding increase to investment funding. This trend, along with ever increasing reporting requirements, continues to make procuring affordable programs a challenge. The vast majority of these programs perform within cost and schedule estimates; however, there continues to be a small set of troubled programs that experience cost overruns and schedule delays. The Department is forced to take money from healthy programs to support these troubled programs, which in turn reduces quantity and capability, and extends program schedules. The

Department must continue to improve its acquisition reform efforts, particularly in high cost programs, to limit the impact to the warfighter.

2-2B. Major Weapon Acquisition	IG Assessment of Progress
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The Department continues to make limited progress in controlling the cost and schedule of major acquisition programs and will have to make critical decisions about which systems should be cut based on competing resources. The Secretary of Defense has, through the last two DoD budgets, made difficult decisions by proposing to end all or part of at least a half dozen major defense acquisition programs that were no longer needed or were poorly performing. Additionally, the Department identified in the Quadrennial Defense Review (QDR) that the Department must improve requirements definition and stop underestimating the costs of weapon systems. The Department must have cost, schedule, and performance realism in the acquisition process while holding the Department and industry accountable.

The Department has revised its policies and guidance to improve its acquisition of weapon systems and address contract management issues. For example, the Department revised its policy governing major defense acquisition programs to provide key department leaders with the knowledge to make informed decisions before a program starts and to maintain discipline once it begins. The revised policy includes the completion of key systems engineering activities before the start of the systems development, a requirement for more prototyping early in programs, and the establishment of review boards to monitor weapon system configuration changes. The Department also issued guidance to address contracting weaknesses and promote the use of sound business arrangements. The Department established a framework for reviewing major services acquisitions, developed guidance on linking monetary incentives for contractors to acquisition outcomes, and implemented regulations to better manage its use of contracting arrangements that can pose additional risks for the Department. The Director, Defense Procurement Acquisition Policy started initiatives to establish an Office of the Secretary of Defense (OSD)-level peer review of proposed contract actions over \$1 billion. The OSD-level peer review involves a 3-day review of the proposed contract action by four independent SES-level personnel. Below the \$1 billion threshold, the Departments are responsible for performing their own peer review of the proposed contract action. These are positive steps, but inconsistent implementation has hindered past DoD efforts to address these high-risk areas. To improve outcomes, the Department must ensure these policy changes and others are consistently put into practice and reflected in decisions made on individual acquisitions.

Congress passed the Weapon Systems Acquisition Reform Act (WSARA) of 2009, which was designed to limit cost overruns, strengthen oversight and accountability, enhance competition and end conflicts of interest. Since the enactment of WSARA, the Department has notably implemented many of the organizational changes required as evidenced by the creation and the appointment of individuals to the following positions: Director, Cost Assessment and Program Evaluation; Director, Developmental Test and Evaluation; Director for Performance Assessments and Root Cause Analyses ; and the Director, Defense Research and Engineering.

In addition, the Under Secretary of Defense for Acquisition Technology and Logistics addressed many of the acquisition process related changes and reporting requirements in a directive type memorandum. While the Department has made some progress, implementation and continued improvement is needed to not only respond to existing shortcomings but to anticipate and address potential future challenges, such as the decreased funding, a diminishing industrial base, or limited acquisition workforce resources.

2-3A. Contracting and the Impact on Decision Making	IG Summary of Challenge
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The DoD acquisition and contracting community is tasked to manage an increasing Defense budget while relying on a smaller, less experienced and inadequately trained workforce. In order to meet the needs of the warfighter and to operate in the existing environment, DoD personnel have had to increase their reliance on contractors. The Department, as the largest purchasing organization in the world, spends about \$400 billion on contracts to non-DoD entities, with the \$400 billion equally divided between products and services. The Department has increasingly turned to contractors to fill roles previously held by government employees and to perform many functions that closely resemble inherently governmental functions, such as contracting support, which includes awarding, and approving contracts and contractual documents, and administering contracts; determining contact requirements, program management, and engineering and technical support for program offices. This reliance on contractors has called into question the proper balance between public and private employees performing agency missions and has increased DoD's vulnerability to contracting fraud, waste, abuse, or misuse of taxpayer dollars.

One way in which the Department coped with the limited resources was to use other agencies' contracting resources. Increasingly, funds were sent to other agencies to perform work for the Department, and in FY 2005, interagency contracting was added to the Government Accountability Office's list of high-risk areas. The Department continues to experience difficulties with the use of interagency contracting. Problems continue to be identified in the areas of source selection determinations, price reasonableness determinations, requirements determinations, surveillance, and justification for using non-DoD contracts.

The Department continues to be challenged to strike a balance between urgent contracting to support the warfighter and performing all of the appropriate acquisition requirements. The effectiveness of contractor support of expanded U.S. operations in Afghanistan and other contingency operations could be hindered by the failure to extract and apply lessons learned from Iraq. Our audits continue to identify weaknesses with requirements definition, source selection, contract monitoring, acceptance of supplies and services, and contract payments.

2-3B. Contracting and the Impact on Decision Making

IG Assessment of Progress

In response to Section 813 of the John Warner National Defense Authorization Act for FY 2007, Public Law 109-364, the Department established a Panel on Contracting Integrity. The Panel, consisting of senior leaders, is focused on eliminating areas of vulnerability in contracting that allow fraud, waste, and abuse. The committee has established subcommittees in the areas of current structure of contracting integrity, sustained senior leadership, capable contracting workforce, adequate pricing, appropriate contracting approaches and techniques, sufficient contract surveillance, contracting integrity in a contingent environment, procurement fraud indicators, contractor employee conflicts of interest, and recommendations for change. The Panel identified 25 actions for implementation in 2010. The Panel reported that many of these actions for implementation were a natural follow-on from those completed in 2009, while others addressed the requirements of the National Defense Authorization Act of FY 2010 and the Weapon Systems Acquisition Reform Act of 2009, and others build upon previous Panel efforts.

On July 26, 2009, in response to the Commission on Wartime Contracting (COWC) in Iraq and Afghanistan's interim report, entitled "At What Cost? Contingency Contracting in Iraq and Afghanistan," June 10, 2009, the Under Secretary of Defense for Acquisition, Technology and Logistics (AT&L) created the DoD Task Force on Wartime Contracting to evaluate the interim report. The COWC interim report contains 55 observations, approximately two-thirds (35) of which relate directly to the 8 issues of immediate concern. The remaining one-third (20) are ancillary (did not directly correlate to an issue of immediate concern). Of the 35 observations, the Department already has significant initiatives underway that address 94 percent of these observations. The Department indicated they are making significant progress on the initiatives with 83 percent (19 initiatives) being free from major challenges. The Department continues to experience barriers in resourcing contingency contracting officer representatives, hiring subject matter experts, and utilizing the services of the Defense Contract Audit Agency.

On June 28, 2010, the Under Secretary of Defense (ATL) issued a mandate to all DoD Acquisition professionals for restoring affordability and productivity in Defense spending. Some initiatives outlined in the mandate include leveraging real competition, use of proper contract type for developments and procurements of goods and acquisition of services, targeting non-value added costs, involving dynamic small business, and rewarding excellent suppliers. In addition to these measures, the mandate addressed strengthening DoD acquisition workforce, improving audits, mandating affordability as a requirement, stabilizing production rates, eliminating redundancy in portfolios, and protecting the technology base.

2. Acquisition Processes and Contract Management

Management's Overall Assessment

The Secretary of Defense established a 23-point plan of action to improve acquisition efficiency in five areas: Target Affordability and Control Cost Growth; Incentivize Productivity and Innovation in Industry; Promote Real Competition; Improve Tradecraft in Services Acquisition; and Reduce Non-Productive Processes and Bureaucracy. The Department is institutionalizing these initiatives, and policy implementation and compliance will be closely monitored. In addition, the Department recently developed a new Joint Contingency Contracting Handbook that provides essential information, tools, templates, and training material to meet the challenges in any contracting environment. In addition, the Department increased its acquisition workforce by 6,200 professionals and continues to work toward the Secretary of Defense's growth goals of 20,000 professionals by FY 2015.

3. Joint Warfighting and Readiness	
3-1A. Joint Warfighting and Readiness	IG Summary of Challenge
<p>The challenge of joint warfighting and readiness is to provide the right force, the right personnel, and the right equipment and supplies in the right place, at the right time, and in the right quantity, across the full range of military operations. This challenge is compounded by the strain on resources because of Operations Iraqi Freedom and Enduring Freedom. Maintaining or increasing the Department's joint warfighting and readiness will require significant resources and continuous management attention. The challenges facing the Department will increase, in both the near- and long-term, as the Department continues the scheduled withdrawal of forces from Iraq and the redeployment of forces to Afghanistan. In the near-term, the Department's execution of the withdrawal in Iraq and redeployment, and the resetting of equipment either for use in Afghanistan or for standing inventory, requires management's continued attention and will present its own challenges to overall joint warfighting and readiness processes. In the long-term, the Department faces the challenge of resetting the Services; retraining skills that have not been required for the current operations; and reengaging with other nations' militaries. This challenge encompasses the need to ensure basic services continue uninterrupted for the members of the armed forces and their families. The DoD's available resources and capabilities are finite and require constant monitoring to enable the Department to operate successfully with the shifting global dynamics. The combination of these various factors continues to challenge the Department. The realignment of forces in the Pacific area of responsibility presents its own set of challenges, including ensuring the Department can maintain its overall readiness posture in the Pacific against the threats it faces. In addition, the realignment of forces requires effective negotiation and relations with the Government of Japan.</p>	
3-1B. Joint Warfighting and Readiness	IG Assessment of Progress
<p>The Department is making progress on the issue of joint warfighting and readiness, but that progress must be monitored to ensure it continues. The Department cannot afford to ignore new and, in some cases, recurring situations that will require attention. For example, although the withdrawal from Iraq is underway, it must be monitored to ensure all equipment and personnel are properly accounted for and only items approved for transfer are transferred. As the Department draws down assets and equipment from Iraq, it must ensure that all units actively participate in the drawdown to ensure accountability and visibility of all equipment, that serviceable material is reused to maximum potential, and ensure the safety of personnel in the field and at receiving activities. This will ensure that the equipment disposition supports either the Department or the coalition forces. Similarly, the increase of forces in Afghanistan must be monitored to ensure forces receive the support required. This includes ensuring that the warfighter, and the civilians and contractors supporting them, have the appropriate protective equipment and that this equipment is properly returned for reset and reuse.</p> <p>Despite a high operating tempo, U.S. Forces are effectively executing their missions globally. Sustained operations in Iraq and Afghanistan impact equipment, the troops, and their families. Forward deployed units are trained, manned, and equipped to accomplish missions. Increased deployments and shorter dwell times impact the readiness of equipment, the troops, and their families. Insufficient dwell time affects readiness of the total force, because it does not allow our troops time to reconnect fully with an important support system – their families. Maintaining readiness, resetting the force during the extended war, modernizing to face future challenges, and allowing troops to reconnect with their families are challenges that the Department and Congress must continually address. The ongoing efforts to relocate service members to Guam and other locations around the globe will enable the armed forces to better shape and focus their force structure in a way that will provide greater flexibility in responding to threats. We have noted, however, that there are substantial Guam infrastructure shortcomings that fall outside of DoD funding authority that could adversely impact the realignment. The Department needs to ensure that interagency planning and execution occur, as these concerns will need to be addressed with additional non-DoD funding. Additionally, competing priorities and the number of contractors available could adversely impact the realignment.</p>	
3. Joint Warfighting and Readiness Acquisition	Management's Overall Assessment
<p>The Department remains focused on ensuring the forces deployed to fight our Nation's wars are trained, equipped, and ready to perform their assigned missions. Our forward-deployed forces are ready, but that readiness often comes at the expense of the non-deployed force readiness. Non-deployed forces often experience less than optimal dwell time and focus their non-deployed training time on their next Iraq or Afghanistan mission</p>	

requirements. This focus, however, can result in forces not being trained for the full spectrum of potential global missions, and combined with the impact of stay-behind equipment and personnel turmoil, can lead to reduced readiness levels. Withdrawing large numbers of troops and equipment from Iraq, while simultaneously increasing force and equipment levels in Afghanistan, is an extremely complex operation. The Department is expending significant effort to ensure this is accomplished in the most effective and cost-efficient manner. We also recognize our obligation to properly take care of our soldiers, sailors, airmen, and Marines -- and their families -- that have carried the burden of extended combat operations, multiple deployments, and the resultant human toll from those efforts. We must be particularly vigilant of those traumatized in our Nation's battles, trauma which can have long-term effects on the individual. The Department is intent on striking the optimal, albeit delicate balance to meet our competing needs in these challenging fiscal times. Key competing challenges include maintaining readiness, resetting the force, structuring the force to meet future threats, modernization, and taking care of our most valuable asset -- our people.

4. Information Assurance, Security and Privacy

4-1A. Risk Management

IG Summary of Challenge

Managing risk continues to be a daunting challenge to the Department. One significant area where the Department must assess the risk that a particular threat will adversely impact its operations is in the acceptance and use of internet-based capabilities. Internet-based capabilities include social networking services, social media, instant messaging, and discussion forums. Commanders at all levels and heads of DoD Components must understand the risks, vulnerabilities, and threats associated with providing access to these internet-based capabilities and implement safeguards and countermeasures to defend against such threats.

4-1B. Risk Management

IG Assessment of Progress

During this past year, the Department has taken steps to address the issues surrounding its use of internet-based capabilities. In November 2009, the IG cancelled its review of DoD compliance with policies and procedures for interactive internet activities. The cancellation occurred to allow the Department to fully address the Deputy Secretary of Defense's requirement to present to the Secretary of Defense the threats and benefits, as well as the policies and processes, to ensure the responsible and effective use of emerging internet-based capabilities. On February 25, 2010, the Deputy Secretary of Defense issued Directive-Type Memorandum (DTM) 09-026, which establishes DoD policy and assigns responsibilities for responsible and effective use of internet-based capabilities, including social networking services.

The DTM provides for the following: (1) The Non-Classified Internet Protocol Router Network shall be configured to provide access to internet-based capabilities across all DoD Components; (2) Commanders at all levels and heads of DoD Components shall continue to defend against malicious activity and deny access to prohibited content and activities via social media; and (3) Use of internet-based capabilities shall comply with paragraph 2-301 of Chapter 2 of the Joint Ethics Regulation. While the Department has postured itself to embrace the benefits of internet-based capabilities in its daily operations, it still faces a challenge of ensuring Commanders at all levels and heads of DoD Components take the appropriate actions to safeguard missions and preserve operations security.

4-2A. Protecting DoD Information

IG Summary of Challenge

One of the most daunting challenges that the Department faces is defending its information and information systems against today's mounting cyber threats. On a daily basis, DoD's information technology infrastructures are continuously attacked by those wanting to not only steal DoD information, but to do harm to DoD programs, operations, and personnel. As the President of the United States has stated, cyber security is one of the most serious economic and national security challenges we face as a Nation. The DoD's major challenge is going to be in centralizing its resources to develop a comprehensive strategy for marshalling its cyber security defenses and implementing policies and procedures to overcome, on an instantaneous basis, any cyber threat.

Another challenge that the Department faces in protecting DoD information is ensuring that its information assurance workforce is properly trained and certified in today's every changing information technology. The members of the information assurance workforce are responsible for protecting information and information systems, and as such, must be trained and certified to a DoD baseline requirement.

In addition, a continuing challenge is to ensure the protection of DoD information in the hands of contractors. The Department must ensure that the diligence and resources it has placed on its internal information and information systems is mirrored by those contractors either running DoD systems or maintaining DoD information on their systems.

4-2B. Protecting DoD Information	IG Assessment of Progress
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In May 2010, the Department took a significant step to address one of its most daunting challenges of defending its information and information systems. The Department announced the establishment of the U.S. Cyber Command, a sub-unified command subordinate to the U.S. Strategic Command. The U.S. Cyber Command will improve DoD's capabilities to ensure resilient, reliable information and communication networks, counter cyberspace threats, and assure access to cyberspace. Service elements, such as the Army Forces Cyber Command, will support the U.S. Cyber Command's mission. While the Department has taken a significant step, challenges remain in centralizing cyberspace operations, developing workable strategies, protecting DoD information networks, and obtaining cyber expertise.

The Department has made progress in meeting the milestones outlined in DoD 8570.01-M, entitled "Information Assurance Workforce Improvement Program," December 19, 2005. As the IG reported in Report No. D-2010-058, "Selected Controls for Information Assurance at the Defense Threat Reduction Agency (DTRA)," May 14, 2010, DTRA had only approximately fifty percent of the required information assurance positions filled with certified personnel. The Department remains challenged to ensure that all information assurance personnel obtain the required certifications in their respective functional areas.

In July 2009, the Department issued DTM 08-027, entitled "Security of Unclassified DoD Information on Non-DoD Information Systems." This was a significant step in the right direction to provide security for all unclassified DoD information on non-DoD information systems. The DTM outlined DoD's policy to incorporate appropriate requirements into all contracts, grants, and other legal agreements with non-DoD entities. In fact, in March 2010, the Department announced the proposed changes to the Defense Federal Acquisition Regulation Supplement (DFARS) in the Federal Register, Volume 75, No. 41. In addition, the Department continued to enhance the Defense Industrial Base (DIB) Cyber Security and Information Assurance Program, established in 2007. Under DoD Instruction 5205.13, dated January 29, 2010, the Department outlined the policy to create a timely, coordinated, and effective partnership with the DIB that would develop standard procedures, for areas, such as contracting and acquisition policy and procedures, to improve the protection of unclassified DoD information on DIB unclassified systems and networks.

Although the Department has made good progress, it still faces the challenge of finalizing changes to the DFARS to implement the DoD requirement for all DoD contractors and their subcontractors to provide adequate security of DoD information in the contractor's and/or subcontractor's possession.

4. Risk Management and Protecting DoD Information	Management's Overall Assessment
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On February 25, 2010, the Deputy Secretary of Defense issued DTM 09-026, which establishes DoD policy and assigns responsibility for effective use of internet-based capabilities, including social networking services. While the Department has postured itself to embrace the benefits of internet-based capabilities in its daily operations, it still faces the challenge of ensuring Commanders at all levels and heads of DoD Components take appropriate actions to safeguard missions and preserve operations security. In May 2010, the Department took a significant step to address its most daunting information security challenge--defending its information and information systems--by announcing the establishment of the U.S. Cyber Command, a sub-unified command subordinate to the U.S. Strategic Command. The U.S. Cyber Command will improve DoD's capabilities to ensure resilient, reliable information and communication networks, counter cyberspace threats, and assure access to cyberspace. Service elements, such as the Army Forces Cyber Command, will support the U.S. Cyber Command's mission. While this is a significant step, challenges remain in centralizing cyberspace operations, developing workable strategies, protecting DoD information networks, and obtaining cyber expertise.

In March 2010, the Department announced proposed changes to the DFARS in the Federal Register, Volume 75, No. 41, that address requirements for safeguarding unclassified information. In addition, the Department continues to enhance the Defense Industrial Base (DIB) Cyber Security and Information Assurance Program, established in 2007. Under DoD Instruction 5205.13, dated January 29, 2010, the Department outlined its policy to create a timely, coordinated, and effective partnership with the DIB to develop standard procedures in areas

such as contracting and acquisition and to improve the protection of unclassified DoD information on DIB-unclassified systems and networks.

5. Health Care

5-1A. Cost Containment

IG Summary of Challenge

The DoD Military Health System (MHS) must provide quality care for approximately 9.6 million eligible beneficiaries within fiscal constraints while facing increased user demands, legislative imperatives, and inflation that make cost control difficult in both the public and private sectors. During a hearing with the Senate Appropriations Subcommittee on Defense, the Secretary of Defense stated the escalating cost of health care is a problem that must be addressed. The DoD budget for health care costs was approximately \$50 billion in FY 2010, an increase of more than 60 percent since FY 2005 (\$31 billion). In addition, the American Recovery and Reinvestment Act of 2009 provides \$0.4 billion for facilities sustainment and \$1.3 billion for construction of hospitals. Another part of the challenge in containing health care costs is combating fraud. Health care fraud is among the top 5 categories of criminal investigations, representing 9.4 percent of the 1,871 open cases of the DoD IG's Defense Criminal Investigative Service at the beginning of FY 2010. Increasing health care benefits also provides additional pressure to manage and contain costs.

5-1B. Cost Containment

IG Assessment of Progress

The DoD MHS has been moving forward on improving health care while attempting to control costs. The MHS implemented the Quadruple Aim Concept, building upon the Institute for Healthcare Improvement's Triple Aim concept that describes the results that can be achieved when all elements of a health care system work together. The MHS uses Quadruple Aim to shape its vision, identifying readiness, population health, experience of care, and per capita cost as the four aims that set the strategic direction to improve mission outcomes. The MHS leadership accepted a value dashboard to monitor implementation of strategic imperatives and serve as good indicators of mission success. The MHS is focusing on many areas to manage per capita costs. Three new TRICARE contracts were awarded in July 2009; however, award protests resulted in staggered implementation of the contracts. The contracts provide incentives for customer satisfaction and include the managed-care support contractors as partners in support of medical readiness.

An internal Assistant Secretary of Defense (Health Affairs) review identified areas that assist in managing costs, to include US Family Health Plan, fraud management, and pharmaceuticals. Additionally, the Quadruple Aim approach to cost control will simultaneously improve quality and reduce cost by focusing on the elimination of unnecessary care, tests, and procedures, and by focusing on delivering health care in the most appropriate setting.

5-2A. Medical Readiness

IG Summary of Challenge

The ability to support and develop the people in the MHS continues to be a challenge. Maintaining medical readiness of the medical staff and units includes ensuring that medical staff can perform at all echelons of operation and that the units have the right mix of skills, equipment sets, logistics support, and evacuation and support capabilities. The challenge of keeping members of the Reserves and National Guard medically ready to deploy continues because of the frequency and duration of deployments.

Increased numbers of returning service members with psychological health issues, along with a shortage of uniformed and civilian mental health workers, will require examination of automated screening tools and improved diagnostics to provide earlier detection and intervention. In addition, addressing the psychological effects of deployment on family members and non-active duty personnel will continue to be a challenge.

5-2B. Medical Readiness

IG Assessment of Progress

The Department published the MHS Human Capital Strategic Plan for 2008 to 2013 and established an MHS Human Capital Strategic Support Office. Quarterly Force Health Protection Survey results show continued improvement in service members' medical readiness, except for the Reserves and National Guard. The MHS is developing strategic imperatives and performance measures under the readiness portion of the Quadruple Aim to increase individual and family medical readiness. The MHS has continued to meet all mission requirements despite very high operational tempo. Data from the Joint Theater Trauma Registry reveal unprecedented

Department of Defense Agency Financial Report for FY 2010

<p>outcomes, including reduction in died of wounds rates and the lowest ever disease non-battle injury rates.</p> <p>The MHS identified psychological health and resiliency as a strategic imperative, with performance measures and goals established for Post-Traumatic Stress Disorder and depression screening, referral, and engagement.</p>	
5-3A. Wounded Warrior Care	IG Summary of Challenge
<p>Strengthening comprehensive and integrated health care from accession through active service, to rehabilitation, and transition to Veterans Affairs (VA) care is a major challenge for the MHS. The number of wounded warriors associated with Southwest Asia and other such conflicts, particularly those affected with Traumatic Brain Injury and Post-Traumatic Stress Disorder, requires diligent management of health care resources. Another related challenge to force health protection and medical readiness is oversight of post deployment health needs, including identifying and managing those requiring care. Although a number of objectives have been identified by the Department and the VA and programs have been initiated, the quality and oversight of these programs must be tightly managed. Transitioning wounded, ill, or injured service members to post-deployment care will grow as a challenge while Overseas Contingency Operations, Operation New Dawn (OND) and OEF, continue. The Department needs to improve the medical care and benefits transition program to achieve a streamlined, transparent, and timely process as wounded warriors move from the DoD system to the Department of VA system.</p>	
5-3B. Wounded Warrior Care	IG Assessment of Progress
<p>The revised MHS strategic plan recognizes continuum of care as a strategic priority concerning the experience of care. Disparities in the transition of health care and benefits were readily identified, yet actionable solutions are difficult to implement and monitor.</p> <p>The Center for the Intrepid in San Antonio, Texas, and the Defense Centers of Excellence for Psychological Health and Traumatic Brain Injury, a network of centers of excellence including the National Intrepid Center of Excellence under construction on the National Naval Medical Center campus in Bethesda, Maryland, provide promising venues to introduce new therapies for amputees, burn victims, and those with traumatic brain injuries and psychological disorders.</p> <p>The Department established the Senior Oversight Council (SOC) in FY 2008 to ensure that all aspects of care, rehabilitation and reintegration for wounded warriors is accomplished. One focus of the SOC is to overhaul the disability processing system and implement improved case management for recovering warriors. The Department is institutionalizing the changes directed by the SOC.</p> <p>The Armed Forces Health Surveillance Center was established to ensure tracking and ongoing surveillance of the health of service members is accomplished in a joint manner and coordinated with Veterans Affairs.</p>	
5-4A. Electronic Health Records	IG Summary of Challenge
<p>Providing information to the right people so they can make informed decisions continues to be a challenge in the health care community. Along with the benefits of expanding automation efforts comes the increased risk to security and privacy of information. The transition from paper to electronic patient records increases the exposure of sensitive patient information to inadvertent or intentional compromise, highlighting the need for appropriate information assurance procedures. Developing and maintaining information operations that ensure the protection and privacy of data will continue to grow as a challenge.</p>	
5-4B. Electronic Health Records	IG Assessment of Progress
<p>The MHS Information Management/Information Technology Strategic Plan for 2010 to 2015 includes the electronic health record as a strategic goal. The goal over the next five years is to focus on improving the electronic health record family of applications to create a comprehensive and reliable system. Specific milestones were established to implement a personal health record prototype and to expand bidirectional sharing of health information between the Department of Defense and the Department of Veterans Affairs; however, DoD has encountered delays in establishing the electronic health record. The DoD continues to progress in sharing electronic medical records with the Department of Veterans Affairs. The final report on the Department and VA joint assessment project recommended that the Departments pursue a common-services approach to sharing inpatient records, which will allow the Department and VA to build upon their already extensive information sharing capabilities. It also will set the stage for the appropriate level of interoperability with other government and private sector organizations.</p>	

Department of Defense Agency Financial Report for FY 2010

5-5A. Implementing BRAC	IG Summary of Challenge
<p>Implementing recommendations resulting from the 2005 Base Realignment and Closure (BRAC) process will continue to be a challenge. In addition to improving the readiness and cost efficiency associated with realigning base structure, a primary objective of the process was to examine and implement opportunities for greater joint activity among the Military Departments. Recapitalization of the physical infrastructure is a challenge, and medical facilities planning for health care on Guam will present additional infrastructure challenges. Military treatment facilities are aging and in need of replacement. Managing funds provided by the American Recovery and Reinvestment Act of 2009 for facilities sustainment, restoration, and modernization projects and new construction will also be a challenge.</p>	
5-5B. Implementing BRAC	IG Assessment of Progress
<p>The BRAC process addresses part of the aging infrastructure, but to fully address the challenge, better standardized data on the condition of facilities is needed. The MHS has begun the multiyear transition and acquisition process of improving capability and access to care in two major and several minor markets. The new Walter Reed National Military Medical Center at Bethesda is expected to be completed in 2011.</p> <p>By establishing more unity of purpose in each of the major markets, the market leaders should be able to distribute resources across hospitals and clinics within a market to meet the needs of the entire population of eligible beneficiaries. In addition, the increased span of control will enable improved continuity of care and coordination of safety and quality programs. In the National Capital Region, the Secretary of Defense established the Joint Task Force National Capital Region--Medical to clarify command and control, and implemented a single manning document categorizing civilian positions as DoD. The Tri-service Medical Education and Training Campus, scheduled to open in phases between 2010 and 2011, should improve the quality and consistency of training for all enlisted, contributing to a culture of jointness and interoperability.</p> <p>Co-locating of the headquarters functions of Health Affairs, the TRICARE Management Activity, the Army Medical Command, the Navy Bureau of Medicine, and the Air Force Medical Service by September 2011 should enhance efforts to achieve unity of purpose for MHS policy, strategy and financial programming and yield greater consistency across the Services in program execution.</p> <p>Several infrastructure issues are addressed through implementation of the American Recovery and Reinvestment Act of 2009. New hospitals are planned at Fort Hood and Camp Pendleton, with construction contracts expected to be awarded by September 30, 2010. In addition, a major renovation at Jacksonville Naval Hospital is funded through the Recovery Act, with the construction contract awarded in December 2009. We currently are reviewing these three major Recovery Act military construction projects. In addition, the DoD IG currently is assessing medical facilities planning in Guam. The results of our review will be reflected in the next management challenges document. The TRICARE Management Activity also has plans for \$400 million of specific Recovery Act facilities sustainment, restoration, and modernization projects to improve medical facilities.</p>	
5-6A. Humanitarian Assistance	IG Summary of Challenge
<p>The Department's expanded role in providing humanitarian assistance and disaster relief to support U.S. strategic objectives and promote human dignity through better health has been identified as a core capability of the MHS, but will continue to provide financial and organizational challenges. The MHS will be challenged to develop a strategy that complements the overall DoD strategy and that interfaces well with other executive agencies, including the Agency for International Development, Department of State, Department of Health and Human Services, and Department of Homeland Security, organizations that traditionally have played the lead role in humanitarian assistance and disaster response.</p>	
5-6B. Humanitarian Assistance	IG Assessment of Progress
<p>Building a bridge to peace through humanitarian assistance and disaster relief is a goal under the MHS strategic plan, in response to Combatant Command goals. The most recent MHS Strategic Plan, covering 2008 through 2010, recognizes many of these challenges and includes a performance metric to measure success in increasing operability with other governmental and non-governmental organizations and international partners.</p>	

5. Health Care	Management's Overall Assessment
<p>The Department is actively working to eliminate unnecessary administrative overhead and unwarranted variation in both its clinical and administrative processes, having set strategic imperatives used in quarterly reviews to ensure targets for both quality and cost are met. This year, particular emphasis is focused on reducing overutilization of emergency rooms, a significant contributor to recent increases in per capita cost.</p> <p>The Department is working with the Reserves and National Guard to address challenges in force readiness, particularly in the area of mental readiness. Recent data shows significant improvement in overall medical readiness. Our human capital team is actively addressing the need for additional mental health services in support of the readiness of the force. Over the past three years, we have added nearly 3,000 new mental health professionals to DoD workforce, and we have greatly expanded the TRICARE network in the area of behavioral health. Deployment of the Patient Centered Medical Home, which includes embedded behavioral health workers in primary care, will add to our capability to address the psychological health needs of service members and their families.</p> <p>The Department is continuously improving care for the wounded, ill and injured, and their families. Since 2007, over 13,000 Service members have enrolled in the integrated disability evaluation system. The Department reduced the disability evaluation period, and service member satisfaction with the process is improving. In addition, the National Intrepid Center of Excellence, which provides specialized services for service members with Post-Traumatic Stress Disorder and traumatic brain injuries, will reach full operating status before the end of the year.</p> <p>In addition, strengthened acquisition structure and processes ensure effective and efficient major acquisitions, such as the Electronic Health Record (EHR). The Department of Defense and the Department of Veterans Affairs are working together to implement the Virtual Lifetime Electronic Record (VLER), with successful pilots now operating at several sites. The VLER vision is to ensure health, benefits, and personnel information of a Service member or Veteran, from the time of accession to interment, is available, as necessary. The MHS is actively working to achieve meaningful use of health information with the rapid implementation of secure messaging and in providing essential health information to patients in digital formats.</p>	
6. Equipping and Training Iraqi and Afghan Security Forces	
6-1A. Iraqi Security Forces	IG Summary of Challenge
<p>Over the next 18 to 24 months, U.S. policy and related DoD military strategy in Iraq will be implemented by aggressive, high-intensity operations that prioritize continuance of the training, equipping, and mentoring of the Iraqi Security Forces (ISF). This will include developing the ISF's logistics sustainment base and conducting a responsible drawdown to 50,000 military forces by August 30, 2010, and all remaining military forces by December 31, 2011. In addition, the Department is faced with transitioning all remaining training, equipping, and mentoring activities to an Office of Security Cooperation under Chief of Mission authority, as well as laying the groundwork for a robust security assistance and Foreign Military Sales program that will endure after the last U.S. military forces leave in December 2011.</p>	
6-1B. Iraqi Security Forces	IG Assessment of Progress
<p>A major national security goal of the U.S. is the establishment of a sovereign, stable, and self-reliant Iraq that contributes to the peace and security of the region and with whom the U.S. can forge a long-term security partnership. An ISF capable of providing for internal security as well as an external defense capability prior to the withdrawal of U.S. Forces from Iraq in December 2011 is essential to achieving these U.S. national objectives.</p> <p>Since the end of FY 2009, in conjunction with the drawdown of U.S. military forces from Iraq, the U.S. has deployed to Iraq newly organized and trained Advisory and Assistance Brigades that focus on stability operations. The mission of these Advisory and Assistance Brigades is to conduct stability and civil capacity building operations; to partner with, enable, and advise the ISF; and if required, conduct full spectrum operations.</p> <p>The U.S. has made progress in developing an ISF logistical system with a capability to sustain independent combat operations. However, this mission objective has not been a command priority until recently, and the window of opportunity to leverage our forces' presence is narrowing. The emphasis on ISF force sustainment underway will require an expedited, intensive push by U.S. Forces-Iraq in order to address the most significant ISF logistical support deficiencies, avert significant degradation of operational readiness, and establish an enduring logistical system before the last U.S. military forces leave on December 31, 2011.</p>	

<p>Considerable progress has been made in developing options and plans for transitioning the U.S. security assistance mission in Iraq to an Office of Security Cooperation under the authority of the Chief of Mission. Effective implementation of those transition plans, however, especially in the areas of manpower, personnel, training and budgeting, could present the U.S. with significant challenges. But, effective transition planning and implementation will help establish a favorable strategic partnership with Iraq.</p>	
6-2A. Afghan National Security Forces	IG Summary of Challenge
<p>Over the next 18 to 24 months, U.S. policy and related DoD military strategy in the Afghanistan-Pakistan region will be implemented by aggressive, high intensity operations that prioritize: continuing the build-up of combat forces in Afghanistan to achieve positive momentum on the battlefield; providing continued training, equipping and mentoring of the Afghan National Security Forces (ANSF) to enable them to assume a leading security operations role; initiating a "conditions-based" drawdown of US combat forces from Afghanistan, beginning the summer of 2011; and developing the capacity of the Pakistan Security Forces to maintain internal security and eliminate extremist Taliban and al-Qaeda forces in the Northwest Frontier safe haven.</p>	
6-2B. Afghan National Security Forces	IG Assessment of Progress
<p>The Afghan government continues to pursue significant expansion of the ANSF, with the support of the international community. Both the Afghan National Army and the Afghan National Police (ANP) may need augmentation in order to win, in partnership with international security forces, the counterinsurgency fight and, ultimately, to develop the capacity to conduct and sustain independent operations.</p> <p>The success of operations in Afghanistan will be partially measured by how well the Afghan population is prepared to provide for, and protect, themselves when U.S. and coalition forces withdraw. The ability to protect themselves will fall on the ANSF, including the ANP. The Department of Defense is assuming responsibility for the training of the ANP from the Department of State (DOS). We reviewed the status of Afghanistan Security Forces (ASF) funds that the Department of Defense provided to the Department of State (DOS) for the training of the Afghan National Police (ANP). Both Departments have agreed to have DoD assume contractual responsibility for the primary ANP training program, which includes Regional Training Centers, basic ANP training, mentoring within the Afghan Ministry of Interior, and the DoD police mentor teams embedded in ANP units in districts throughout Afghanistan. The Department of State did not maintain adequate oversight of Government-furnished property; maintain contract files as required by the Federal Acquisition Regulation; always match goods to receiving reports, or follow internal control procedures requiring in-country contracting officer's representatives to review contractor invoices to determine if the costs were allowable, allocable, or reasonable prior to payment, and to validate deliverables. We were unable to determine if DOS expended Afghanistan Security Forces funds provided by the Department of Defense in accordance with Congressional intent. We identified \$80 million in expired ASF funds that the DOS had not returned to DoD or the U.S. Treasury. The DOS and DoD have not provided enough resources to adequately train members of the Afghan Women's Police Corps.</p> <p>As the program transitions, there is risk that all ongoing efforts be accurately identified and transferred. There will be continued risk that the program evolve as needed to address the changing security environment in Afghanistan. The program was originally envisioned to provide security forces capable of performing traditional law enforcement duties. As the security situation in Afghanistan deteriorated, the program needed to include more paramilitary-type security skills as well as traditional law enforcement. The Department must be fluid in its ability to change the program as needed to adapt to this changing environment.</p>	
6. Equipping and Training Iraqi and Afghan Security Forces	Management's Overall Assessment
<p>The DoD objective between now and December 2011 is to develop an ISF capable of providing internal security as well as a minimal foundation for external defense. Following the withdrawal of U.S. forces from Iraq in December 2011, the ISF will continue to mature in their leadership roles providing security and overall stability for the citizens of Iraq. The citizens of Iraq continue to develop their confidence in the ISF, and it is becoming clear that the growing professionalism of the ISF is a source of national pride.</p> <p>A key strategic focus remains on training, equipping, and partnering with the Afghan National Security Forces (ANSF) to enable the transition of lead security responsibility to the Government of Afghanistan and initiate a "conditions-based" redeployment of U.S. combat forces, beginning in July 2011, with the ANSF being in the lead by 2014.</p>	

The North Atlantic Treaty Organization (NATO) and the Government of Afghanistan continue to grow both the quality and quantity of the ANSF. Both the Afghan National Army (ANA) and the Afghan National Police (ANP) still need support from the international community—particularly in pledging institutional trainers for the ANSF and Operational Mentoring and Liaison Teams (OMLTs) and Police Operational Mentoring and Liaison Teams --to train the ANSF and provide mentors and partners in the field.

As of August 2010, both ANA and ANP force levels were well above target goals, at approximately 136,000 and 120,000, respectively. The NATO Training Mission-Afghanistan (NTM-A) implemented several positive changes in the ANSF training regime since November 2009, including increasing the number of trainers, providing better marksmanship training, adding literacy training, and opening branch schools for higher end training. Still, challenges remain, including Officer and Non-Commissioned Officer shortages.

7. Nuclear Enterprise

7-1A. Decline of Focus on the Nuclear Enterprise

IG Summary of Challenge

The Department faces complex and long-standing nuclear enterprise management challenges that affect DoD's ability to provide public assurance that it can meet its nuclear operational and surety responsibilities. A 2008 Defense Science Board report states that since the end of the Cold War, there has been a marked but gradual decline in the level and intensity of focus on the nuclear enterprise and the nuclear mission. When comparing the current level of focus to that of 1990, the aggregate change is dramatic.

The decline is characterized by:

- Embedding nuclear mission forces in non-nuclear organizations.
- Markedly reducing levels of leadership whose daily focus is on nuclear enterprise.
- Generally devaluing the nuclear mission and those who perform the mission.

Numerous reports and studies issued over the past decade have documented the decline. From 1991 to 2009, the IG identified and reported on aspects of this decline in a series of classified audit reports related to the security of nuclear systems. Although specific report details are classified, the weaknesses identified in each of those reports are a direct result of the decline in emphasis of the nuclear enterprise and mission.

7-1B. Decline of Focus on the Nuclear Enterprise

IG Assessment of Progress

The Department has continued to sustain its focus to renew the nuclear enterprise. In September 2009, the DoD IG issued a report on DoD actions in response to the recommendations contained in the Commander Directed Report of Investigation Concerning an Unauthorized Transfer of Nuclear Warheads Between Minot AFB, North Dakota, and Barksdale AFB, Louisiana, August 30, 2007; the Air Force Blue Ribbon Review of Nuclear Weapons Policies and Procedures, February 8, 2008; and the Defense Science Board Permanent Task Force's "Report on the Unauthorized Movement of Nuclear Weapons;" and the DoD IG found that the Department is taking actions to address those report recommendations.

The Department has continued to analyze and study critical elements of the nuclear enterprise. In addition to the three reports noted earlier, the Department has issued numerous additional reports related to the nuclear enterprise, including:

- Nuclear Surety Staff Oversight of US Air Force Nuclear Surety Inspections, April 1, 2008
- Air Force Inventory and Assessment: Nuclear Weapons and Nuclear Weapons-Related Materiel, May 25, 2008
- Air Force Comprehensive Assessment of Nuclear Sustainment, July 26, 2008
- SECDEF Task Force on DoD Nuclear Weapons Management, Phase II, September 12, 2008
- Air Force Nuclear Task Force (Nuclear Roadmap), October 24, 2008
- Nuclear Weapons Management, January 8, 2009

During FY 2011, the DoD IG will begin a review of DoD actions in response to these additional reports.

Joint Chiefs of Staff. In March 2010, in response to the reports on the decline in focus on the nuclear enterprise, the Chairman of the Joint Chiefs of Staff approved a comprehensive reorganization of the Joint Staff Operations Directorate to add a new Deputy Director for Command, Control, and Nuclear Operations. This reorganization placed a single General Officer in a position to oversee all aspects of nuclear operations for the Chairman. This new Deputy Directorate was officially stood up on October 1, 2010. Additionally, the Chairman approved a reorganization of the Joint Staff Strategic Plans and Policy Directorate to add a new Deputy Director for Strategic Stability, effective September 1, 2010, to oversee all aspects of nuclear and weapons of mass destruction for the Chairman.

Department of the Air Force. On August 7, 2009, the United States Air Force activated the Air Force Global Strike Command. Its mission is to “Develop and provide combat-ready forces for nuclear deterrence and global strike operations – Safe, Secure, Effective - to support the President of the United States and combatant commanders.” The Command assumed the nuclear capable assets of Air Force Space Command on December 1, 2009, and Air Combat Command on February 1, 2010. The activation of the Air Force Global Strike Command is a significant step in the Air Force’s efforts to reinvigorate the Air Force Nuclear Enterprise.

The Air Force also established the Nuclear Oversight Board, whose charter is to oversee and drive structural, procedural and cultural enhancements to the Air Force Nuclear Enterprise. Chaired by the Secretary of the Air Force and the Chief of Staff of the Air Force, this group brings together Air Force senior leaders to address and resolve nuclear mission issues. Additionally, the Air Force established the Assistant Chief of Staff Strategic Deterrence and Nuclear Integration to integrate all aspects of nuclear policy, operations, and sustainment across the Air Staff and has enhanced the Air Force Nuclear Weapons Center to ensure sustainment of Nuclear Enterprise systems.

The Air Force has created policy and procedures to manage, process, and assess Nuclear Weapon Reserve Material and an account for it through an automated supply chain system called Positive Inventory Control Fusion. Additionally, the Air Force consolidated Nuclear Weapon Reserve material storage facilities and reduced unnecessary fielding in operational bases.

Department of the Navy. Following the Defense Science Board investigation of unauthorized movement of nuclear weapons between Minot AFB and Barksdale AFB, the Department of the Navy independently undertook internal assessments to evaluate the state of the Navy’s nuclear enterprise. In May 2008, the Secretary of the Navy directed Strategic Systems Programs (SSP) to conduct a comprehensive Self-Assessment. The Secretary also directed Naval Reactors to conduct an audit and review of the Self-Assessment and a broad review of operations within the Navy’s Nuclear Weapon Enterprise. SSP’s Self Assessment indicated that the Navy was operating at a satisfactory level with respect to Nuclear Weapons management, but identified six areas that were deemed in need of some improvement. Naval Reactors’ subsequent audit report stated that the Review Team “found the Navy’s nuclear weapons and related Components to be controlled and managed in an overall satisfactory manner, with some areas identified that required improvement. The Review Team did not identify any findings that would affect the health and safety of the public.” Additionally, in June 2008, the Secretary of Defense (SECDEF) appointed a Task Force to address the nuclear mission of the Air Force (Phase I) and the nuclear mission of the DoD overall (Phase II). The Phase II report (Schlesinger Report) defined policy, organizational and procedural issues that needed to be addressed across DoD in order to retain disciplined and effective nuclear forces. The Task Force found that the Navy has maintained its commitment to the nuclear mission, although there was evidence of some “fraying around the edges” and made recommendations to ensure a credible nuclear deterrent now and for the foreseeable future.

Other Actions. In December 2009, the Federal Advisory Committee for the Nuclear Command and Control System Comprehensive Review issued its final report. This classified report contains findings and recommendations to address issues related to U.S. Nuclear Command and Control System. The DoD IG will monitor DoD progress in addressing the issues raised in this report.

In April 2010, the Department issued the Nuclear Posture Review report, which establishes the nuclear policy, strategy, capabilities, and force protection for the next five to ten years. Among other reasons, this report is crucial for establishing requirements and funding priorities for the nuclear enterprise.

In our view, the Department has undertaken significant actions to reverse the decline and reinvigorate the nuclear enterprise. Sustained commitment and funding will be required to maintain the momentum of the current efforts.

7-2A. Incidents Indicate Systemic Problems	IG Summary of Challenge
<p>During FY 2008, the Department experienced a series of incidents that indicated significant problems with nuclear enterprise management. Failure to follow prescribed verification procedures resulted in nuclear warheads being inadvertently transferred from Minot Air Force Base (AFB) to Barksdale AFB. Sensitive missile components were erroneously shipped to Taiwan. The 5th Bomb Wing at Minot AFB failed a nuclear surety inspection and had to be re-inspected to a satisfactory rating. Despite improvement in many areas, systemic challenges still remain.</p>	
7-2B. Incidents Indicate Systemic Problems	IG Assessment of Progress
<p>Although the Department has undertaken significant efforts to reinvigorate the nuclear enterprise, significant issues continue to arise. Security continues to be a major issue for the DoD Nuclear Enterprise. During the past 12 months, unauthorized personnel have twice gained access onto NATO military installations. While U.S. personnel and munitions were never at risk, and nuclear security was not compromised, the incidents do illustrate the importance of the Department continuing to maintain focus on security and force protection issues.</p> <p>In September 2009, the DoD IG issued a "Report on the B-61 Nuclear Weapon Use Control" which contained recommendations on funding the B-61 Life Extension Program. The Air Force concurred with report recommendations. After our report was issued, the Nuclear Posture Review validated the requirement for the B-61 Life Extension Program. The DoD IG recently completed fieldwork on a review of "Sustaining the Weapons Storage and Security System" and will make recommendations for improving maintenance and addressing spare parts issues. Addressing the maintenance issue will be critical to support the Nuclear Posture Review long-term goal of continuing to field the B-61 weapon.</p> <p>In February 2010, the Office of the Deputy Assistant to the Secretary of Defense for Nuclear Matters provided the DoD IG with a briefing on the status of the DoD Nuclear Weapons Physical Security Roadmap for addressing physical security issues. The briefing indicated that the Department is making significant progress. During FY 2011, the DoD IG will begin a follow-up audit of its 2002 report on Physical Security of Nuclear Weapons Located in the Continental United States. During this audit, we will assess DoD progress in addressing the physical security issues and determine if there are any impediments.</p> <p>The Air Force has taken actions to improve the inspection process. The Air Force Inspection Agency now conducts 100% oversight of all Nuclear Surety Inspections. The Air Force Inspection Agency stood up a centralized core team of inspectors that integrates Major Command (MAJCOM) Inspector General teams, which should provide a more consistent application of inspection standards and ensuring root-cause for issues are determined and shared across the Air Force. Additionally, the Nuclear Inspection Enterprise stood up a Nuclear Surety Inspection Review Group, which meets semi-annually to discuss pertinent inspection issues and ensure consistency and standardization across the Nuclear Inspection Enterprise.</p> <p>In 2008, the Department of the Navy established the OPNAV Nuclear Weapons Council (ONWC) and Navy Nuclear Weapons Senior Leader Oversight Council (SLOC) to coordinate all OPNAV staff responsibilities for nuclear weapons activities and to coordinate and strengthen ties between Navy's nuclear weapon operations, material support, and oversight functions. These two councils are being consolidated into a single Navy Nuclear Weapons Oversight Council (NNWOC). One of the focus areas for NNWOC is addressing recommendations for the Navy from the Schlesinger and Naval Reactors reports by approving corrective actions and closure plans. Additionally, the Navy's Strategic Systems Programs established Oversight and Compliance Offices in Kings Bay, GA and Bangor, WA to fulfill Director, Strategic Systems Programs responsibility across the nuclear weapons surety spectrum of operations.</p>	
7-3A. Keys to Improvement	IG Summary of Challenge
<p>The Department needs to sustain its focus on the nuclear enterprise. The following elements are key to improvement:</p> <ul style="list-style-type: none"> • Create an environment that emphasizes the nuclear mission and that a reliable, safe, secure, and credible nuclear deterrent is essential to national security and is a high DoD priority. • Conduct detailed reviews and studies of all critical elements of the nuclear enterprise to identify key deficiencies and methods for improvement. • Develop corrective action plans that correct the deficiencies and provide adequate funding and leadership to ensure implementation. 	

<ul style="list-style-type: none"> Implement the corrective actions and conduct follow-up reviews to ensure that the action plans are correcting the deficiencies. 	
7-3B. Keys to Improvement	IG Assessment of Progress
<p>The Department has taken significant action to conduct detailed reviews and studies of critical elements of the nuclear enterprise to identify key deficiencies and methods for improvement. Additionally, they are implementing report recommendations and developing corrective action plans that correct the deficiencies.</p> <p>We fully support these efforts. However, successfully addressing the deficiencies in the nuclear enterprise will require years of sustained effort. Fixing the problems will require commitment, effort, and resources. The IG will monitor DoD's progress in implementing the various report and study recommendations.</p>	
7. Nuclear Enterprise	Management's Overall Assessment
<p>The Department continues to make substantial progress in improving the nuclear enterprise. The Department has taken positive action to address recommendations made in IG and other oversight reports, conducted reviews of the enterprise to identify and correct deficiencies, and created new management structures, such as the Air Force Global Strike Command. In addition, the release of the Nuclear Posture Review and the Section 1251 Report to Congress on DoD plans for the nuclear deterrent over the next ten years have provided an overarching path forward for sustaining the nuclear enterprise. The Department remains fully committed to restoring confidence in the nuclear enterprise and in the safe handling and accountability of DoD nuclear assets. While success in accomplishing this task will require years of sustained commitment, the Department will continue to engage in a robust effort to implement report recommendations and corrective action plans to address deficiencies.</p>	
8. American Recovery and Reinvestment Act (ARRA)	
8-1A. American Recovery and Reinvestment Act	IG Summary of Challenge
<p>In passing the American Recovery and Reinvestment Act (ARRA) of 2009, commonly referred to as the Recovery Act (Public Law 111-5), the Congress provided supplemental appropriations to preserve and create jobs; promote economic recovery; assist those most affected by the recession; provide investments to increase economic efficiency through technological advances in science and health; and invest in transportation, environmental protection, and other infrastructure. Under the Recovery Act, Congress appropriated \$7.4 billion to the Department for the following programs:</p> <ul style="list-style-type: none"> Facilities Sustainment, Restoration, and Modernization (\$4.26 billion) Military Construction (\$2.18 billion) Near Term Energy-Efficient Technologies (\$300 million) Energy Conservation Investment (\$120 million) Homeowners Assistance Program (\$555 million) <p>The United States Army Corps of Engineers (USACE) received a \$4.6 billion appropriation for its civil works program. The \$4.6 billion provided for the civil works program included \$2 billion for construction and \$2.075 billion for Operations and Maintenance.</p> <p>The Recovery Act also provided unprecedented efforts to ensure the responsible distribution of funds for the Act's purposes, and transparency and accountability for expenditures, so that the public would know how, when, and where tax dollars were being spent. Further, the Recovery Act stated that the President and the heads of Federal departments and agencies were to manage and expend the funds made available in the Act to achieve its purpose, which included commencing expenditures for activities as quickly as possible, consistent with prudent management.</p> <p>The Department is pursuing three broad goals with Recovery Act Funding: preserve and create American jobs, care for U.S. Service members and their families, and improve DoD energy efficiency. The Department intends to expend DoD funds as quickly as possible on facilities sustainment, restoration, and modernization, military construction, energy conservation, near-term energy efficiency technology demonstration and research, and homeowners' assistance. Specific investments in military construction will further the goal of providing stimulus to the economy while helping to improve the quality of life for the troops and their families.</p>	

By September 30, 2010, the Department plans to have started 4,700 construction and facility repair projects (meaning contract award and construction/repair work had commenced) using \$6.5 billion of the Recovery Act funds. The Department is planning on over 4,488 repair projects, totaling \$4 billion for installations in all 50 states, two territories and the District of Columbia. An additional \$1.785 billion is available for new construction, including \$1.33 billion for replacement of aging hospitals, \$115 million for family housing construction, \$240 million for 21 Child Development Centers, \$100 million for two Warrior in Transition facilities. In addition, \$555 million of Recovery Act Homeowners Assistance funds are available to reduce the impact of the downturn in the housing market on military members and civilians. The Department is using \$120 million in Recovery Act funds for 45 energy efficiency projects and an additional \$300 million for 51 energy programs researching ways to reduce DoD's energy demand via increasing fuel efficiency or advancing new technologies related to alternative energy sources.

The USACE list of Recovery Act-funded Civil Works projects valued at \$4.6 billion includes approximately 172 construction projects, 523 Operation and Maintenance projects, 45 Mississippi River and Tributaries projects, 64 Investigations projects, and nine projects under the Formerly Utilized Sites Remedial Action Program. Regulatory Program funds are distributed to USACE districts based upon workload. The projects selected represent a set of productive investments that will contribute to economic development and aquatic ecosystem restoration.

The Department continues to place an emphasis on meaningful and effective competition to get the best deal for the warfighters and the taxpayers. Given the importance of the Recovery Act dollars in stimulating the economy, the Department has taken extra steps, including frequent communications with Senior Procurement Executives (SPEs), regarding the expectations for contract implementation. SPEs in the Department are communicating more frequently with their respective acquisition workforce, including flash notices and reminders of Recovery Act regulations, specifically the importance of competition. The Department in responding to a Recovery Accountability and Transparency Board's survey of contract workforce staffing, indicated that their Acquisition Workforce staffing was less than adequate to handle the additional requirements from the Recovery Act and those staffing shortages would impact both Recovery and non-Recovery Act work.

The Recovery Act also established unprecedented efforts to provide transparency and accountability of expenditures so that the public would know how, when, and where tax dollars were being spent. The reporting requirements by recipients of DoD Recovery Act awards and by Federal agencies and departments on the use of Recovery Act funds are contained in legislation, regulations, and Office of Management and Budget (OMB) guidance. The OMB interim guidance clarifies the responsibilities of Federal contractors and agency officials regarding Federal contracts that use Recovery Act funds. The guidance requires agencies to review contractor reports to ensure the information provided in the report is consistent with the award. Further, OMB interim guidance stipulates that agencies are to have oversight processes in place to review contractor reports and to conduct limited reviews intended to identify significant errors or material omissions in the reports. The Department had established processes to perform limited data quality reviews intended to identify material omissions and/or significant reporting errors and to notify the recipients of Recovery Act funds of the need to make appropriate and timely changes.

8-1B. American Recovery and Reinvestment Act	IG Assessment of Progress
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The OMB specified the initial step for each agency receiving Recovery Act funds to take was to develop formal documented plans identifying how the recovery funds will be applied and managed. OMB required that agencies discuss both Recovery Act goals and how different parts of the agency are coordinating efforts toward successful implementation and monitoring of these goals; required agencies to submit separate plans for each program funded by the Recovery Act; and stipulated 12 minimum requirements that each plan must address. The DoD Agency Plan and four program-specific plans met the 12 minimum OMB requirements. We did not review the Homeowners Assistance Program (HAP) plan but have initiated an audit of actual DoD HAP program claims and payments. The review will continue into FY 2011.

In our 2009 IG Assessment of Progress for this management challenge area, we noted that DoD's execution of the \$12 billion of Recovery Act funds was not moving as quickly as the Department had planned, and much of the spending and actual work on the projects would occur in FY 2010. The DoD Recovery Act funds for facility repair and research and development projects, valued at \$4.26 billion, would expire for obligation at the end of FY 2010. The DoD continued to press forward to obligate these funds and, as of September 30, 2010, with the aid of a statutorily directed \$260.5 million ARRA rescission, the Department obligated 99.9 percent of the remaining \$4 billion in expiring funds. The Department also achieved its goal of expending at least 45 percent of all ARRA

funds by the end FY 2010. Funds for new construction are available for obligation until FY 2014. As of September 30, 2010, the Department had obligated 71 percent of these funds. The continuing pressure to commence activities and expend Recovery Act funds as quickly as possible, consistent with prudent management, will add pressure to DoD's understaffed contracting professionals to award and administer contracts in an expedited manner.

In addition, contractors who are awarded these contracts must also satisfy the new Recovery Act reporting requirements. Recipients of Recovery Act funds must submit estimates of jobs created and jobs retained for each Recovery Act project or activity during each fiscal year quarter. The Department must ensure the accuracy and timeliness of the recipient's reports. Our initial FY 2010 reviews of DoD and USACE recipient reporting internal controls found that the Department did not have a well-defined process to perform limited data quality reviews intended to identify material omissions and/or significant reporting errors and to notify the recipients of the need to make appropriate and timely changes. Nor did the Department have specific policies and procedures to perform these tasks. Conversely, USACE had developed processes to perform limited data quality reviews for its Civil Works Programs but these processes did not completely and adequately identify errors in recipient reported data, or establish adequate logic checks to validate "the number of jobs created" reported by recipients. We are continuing reviews of DoD and USACE controls over recipient reporting.

Without adequate and continuous management attention to Recovery Act implementation, especially contractor oversight and recipient reporting, the Department will have a recurring challenge to effectively meet the intent of the Recovery Act and maintain adequate transparency, accountability, and stewardship of taxpayer funds.

8. American Recovery and Reinvestment Act

Management's Overall Assessment

The Congress initially appropriated \$7.4 billion in ARRA funds to the Department. With a statutorily-directed \$260.5 million rescission, the Department received a net amount of \$7.2 billion in Recovery Act funds. Through September 30, 2010, the Department of Defense awarded \$6.5 billion in Recovery Act funds, over 90% of the \$7.2 billion in ARRA funds allocated to the Department. These \$6.5 billion in awards include the \$4 billion allotted for Facilities Sustainment, Restoration, and Modernization projects, the \$0.3 billion allotted for Near Term Energy-Efficient Technologies projects, and \$1.7 billion (74%) of the \$2.3 billion allotted for Military Construction or Energy Conservation Investment projects, funds that are available for obligation through September 30, 2014. The obligations for Military Construction or Energy Conservation Investment projects and project completions in all programs will continue to increase throughout FY 2011.

The President established high standards of transparency and accountability for the use of Recovery Act funds. Since the signing of the ARRA, the Department has worked closely with OMB and other White House offices to effectively implement award and reporting requirements. The Secretary of Defense designated the Principal Deputy Under Secretary of Defense (Comptroller) to serve as DoD's primary point-of-contact to the White House. A DoD Senior Steering Committee monitors ARRA program implementation, establishes policies and procedures, and reviews key metrics as funds are obligated and executed.

The OUSD(C) uses its centralized Business Enterprise Integration System (BEIS) to track the obligation and execution of ARRA funds at the project-level, which ensures compliance with the financial management policies pertaining to the Recovery Act. Also, the Department established performance measures, supported by standardized definitions, quantifiable outputs, and designated measurement frequencies, to monitor execution of the funds. These measures include:

- Percent net change of child development center slots, barracks bed spaces, and family houses created;
- Change in facility condition;
- Number of families aided by Homeowners Assistance funding; and
- Estimated annual energy savings.
- Results of these performance measures are updated and readily accessible on the DoD ARRA public website, www.recovery.gov and www.defense.gov/recovery.

In response to unprecedented requirements to inform the public as to the use of ARRA funds and ensure transparency and accountability of expenditures, the Department issued guidance entitled, "Posting Pre-Solicitation and Award Notices, Reporting Contract Actions, and Reporting Performance Assessments for Actions Funded by the American Recovery and Re-Investment Act of 2009," on March 13, 2009. Also, on July 6, 2009, DoD issued guidance entitled "Use of the Purchase Card – American Recovery and Reinvestment Act (ARRA)," to ensure the transparency of card transactions via required reporting.

In addition, recipients who received contracts funded with ARRA dollars are responsible for reporting this award information, including number of jobs generated, on a public website. These recipient reporting requirements are contained in legislation, regulations, and OMB guidance. On December 16, 2009, the Department issued initial guidance, entitled "Guidance on Reviewing Contractor Reports Required by the American Recovery and Reinvestment Act of 2009," that established DoD quality review processes to validate recipient reports and identify significant errors or material omissions in the recipients' reports. Subsequent to issuing this guidance, OMB issued several policy updates in this area. To minimize proliferation of multiple policy memoranda, the Department uses OMB-issued guidance to validate the accuracy and completeness of recipient reports. To increase the accuracy of the recipient's reports, the Department provided each ARRA recipient with a partially completed reporting template, entitled "Key Award Information for Contractor Reports," that identified various federal procurement and/or accounting data and codes recipient were required to report on the public website. These templates greatly increased the accuracy of recipient reports, as this data and coding is not typically understood or known to the contractors. The Department also created a website that provides guidance to contractors and reviewers (<http://www.acq.osd.mil/dpap/pdi/eb/arra.html>). This website contains key information required for successful implementation of recipient reporting, along with a direct link to the OMB FAQ webpage for up-to-date guidance and direction.

MANAGERS INTERNAL CONTROL PROGRAM

The OUSD(Comptroller) leads DoD's Federal Managers' Financial Integrity Act (FMFIA) program, designated as the Managers' Internal Control Program (MICP). The MICP holds managers throughout the Department accountable for ensuring effective internal management controls in their areas of responsibility. All Components are required to conduct a robust programmatic approach to establish and assess internal management controls for all non-financial, mission-essential operations. Components that produce stand-alone financial statements are also required to include financial reporting assurance in their programs.

Financial Statement Material Weaknesses

The following Table 1 lists the DoD IG-identified 13 material weaknesses in financial statement reporting.

Table 1. Summary of Financial Statement Audit						
Audit Opinion: Disclaimer						
Restatement: Yes						
	Material Weakness	Beginning Balance	New	Resolved	Consolidated	Ending Balance
1	Accounts Payable	1				1
2	Accounting Entries	1				1
3	Environmental Liabilities	1				1
4	Government Property in Possession of Contractors	1				1
5	Intragovernmental Eliminations	1				1
6	Operating Materials and Supplies	1				1
7	Reconciliation of Net Cost of Operations to Budget	1				1
8	Statement of Net Cost	1				1
9	Financial Management Systems	1				1
10	Fund Balance with Treasury	1				1
11	General Property, Plant & Equipment	1				1
12	Inventory	1				1
13	Accounts Receivable	1				1
Total Material Weaknesses		13	0	0	0	13

Types of Material Weaknesses

The DoD management-identified weaknesses are determined by assessments of internal management controls, as required by the FMFIA and OMB Circular No. A-123, and fall into three categories:

1. FMFIA Section 2, Financial Reporting Material Weaknesses (see Table 2a).
2. FMFIA Section 2, Non-Financial Operations Material Weaknesses (see Table 2b).
3. FMFIA Section 4, Financial System Nonconformance Weaknesses (see Table 2c).

The Department began FY 2010 with 17 outstanding material weaknesses, and during the year added two new material weaknesses, for a total of 19 material weaknesses at year end. Tables 2a, 2b, and 2c identify the resulting management-identified weaknesses.

1. FMFIA Section 2, Financial Reporting Material Weaknesses. Under the oversight of the DoD Senior Assessment Team, DoD’s assessment of financial reporting identified the following material weaknesses, listed in Table 2a, which previously have been reported. The column entitled "Ref Table 1" crosswalks the reported FMFIA manager-identified weaknesses to similar weaknesses identified by the IG, which are listed in Table 1.

Table 2a. Effectiveness of Internal Control Over Financial Reporting (FMFIA Section 2)							
Statement of Assurance: No Assurance							
Material Weaknesses	Ref Table 1	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
1. Military Equipment Assets	11	1					1
2. Real Property Assets	11	1					1
3. Environmental Liabilities	3	1					1
4. Health Care Liabilities		1					1
5. Fund Balance with Treasury	10	1					1
6. Accounts Receivable	13	1					1
7. Inventory	12	1					1
8. Operating Materials and Supplies	6	1					1
9. Accounts Payable	1	1					1
10. General Purpose Equipment	11 & 4	1					1
11. Financial Reporting Compilation	2, 7, & 8	1					1
12. Financial Reporting of Intragovernmental Eliminations	5	1					1
Total Financial Reporting Material Weaknesses		12					12

Table 2a-1 provides the description and corrective action plan for each material weakness related to internal controls over financial reporting.

Table 2a-1 FY 2010 Internal Control Over Financial Reporting Material Weaknesses (1 of 4)					
	Material Weaknesses	Year Identified	DoD Components	Corrective Actions	Target Correction Date
1	Military Equipment Assets: The DoD's financial systems do not support capturing and recording the historical cost of military equipment in order to comply with accounting standards.	FY 2003	OUSD(AT&L); Army; Navy; SOCOM ¹	Components are following a strategy to first validate the existence and completeness of mission-critical asset records in logistics and accounting systems. Upon confirmation of the accuracy of item counts in property records, Components will implement controls and processes to value military equipment using transactional data or estimates, as appropriate.	FY 2016
2	Real Property Assets: The Department does not have adequate internal controls in place to provide assurance that real property assets are identified and properly reported in its financial reports. The Department, the Military Services, and applicable Defense Agencies are addressing these areas.	FY 2003	OUSD(AT&L) ² ; SOCOM; Navy; NGA; Air Force; Army; DLA; MDA	Components are implementing sustainable real property, physical and fiscal accountability business processes, and consistent management controls. They are also completing a Department-wide real property reconciliation that will validate existence and completeness by verifying system data to location of physical assets.	FY 2014
3	Environmental Liabilities: DoD's internal controls for reporting environmental liabilities do not provide assurance that clean-up costs for all of its ongoing, closed, and disposal operations are identified, consistently estimated, and appropriately reported.	FY 2001	Air Force; Army; USACE ³	Using OUSD(AT&L) guidance, Components are validating the completeness of the environmental liability universe and ensuring liability estimates are supported with adequate audit trails and documentation.	FY 2012
¹ SOCOM: Special Operations Command ² OUSD(AT&L): Office of the Secretary of Defense (Acquisition, Technology, and Logistics) ³ USACE: U.S. Army Corps of Engineers					

Table 2a-1 FY 2010 Internal Control Over Financial Reporting Material Weaknesses (2 of 4)					
	Material Weaknesses	Year Identified	DoD Components	Corrective Actions	Target Correction Date
4	Health Care Liabilities: The current military health system financial processes cannot collect sufficient transaction-level cost and performance information regarding procedures performed in military treatment facilities to support reliable financial reports.	FY 2003	MERHCF ¹ ; SMA ²	Medical Components are implementing procedures to improve procedure coding and financial reconciliation for military treatment facilities' operations as well as developing proposals to reimburse military treatment facilities on a per capita basis. Such proposals would be similar to arrangements with managed-care providers. Implementation of Service ERPs will also improve overall financial reporting.	FY 2017
5	Fund Balance with Treasury: The Department is unable to reconcile transactions posted to its Fund Balance With Treasury (FBWT) general ledger accounts with transactions reported to and posted to Department of the Treasury's accounts.	FY 2006	DIA ³ ; DLA ⁴ ; Air Force; Navy; SMA; Army; CBDP ⁵ ; SOCOM ⁶	Components will work toward integrating compliant target systems with feeder systems to maintain transaction-level supporting documentation for disbursements and collections. Components also are developing the processes and controls to reconcile transaction-level differences between Treasury and Department accounts in a timely, efficient manner.	FY 2017
6	Accounts Receivable: The Department is unable to accurately record, report, collect, and reconcile intragovernmental accounts receivable as well as accounts receivable due from the public.	FY 2003	DLA; SMA; Air Force; Army	Components are continuing efforts to implement ERP systems to improve collections of payments and minimize manual processes. Improving reconciliations between systems, to include identification of aging accounts, is another key aspect of the DoD efforts to resolve this weakness.	FY 2017
<p>¹ MERHCF: Medicare Eligible Retiree Health Care Fund ² SMA: Service Medical Activity ³ DIA: Defense Intelligence Agency ⁴ DLA: Defense Logistics Agency ⁵ CBDP: Chemical and Biological Defense Programs ⁶ SOC: Special Operations Command</p>					

Department of Defense Agency Financial Report for FY 2010

Table 2a-1 FY 2010 Internal Control Over Financial Reporting Material Weaknesses (3 of 4)					
	Material Weaknesses	Year Identified	DoD Components	Corrective Actions	Target Correction Date
7	Inventory: The Department is unable to accurately account for, value, and report inventory on DoD's financial statements.	FY 2003	Navy; DLA ¹ ; Army; Air Force; Navy	Department efforts to improve accounting for inventory focus on ensuring adequate documentation exists to support consistent, accurate in-transit inventory valuations, tracking of inventory and visibility of inventory. The ability to identify and implement proper inventory sampling methodologies is also an important element.	FY 2016
8	Operating Materials and Supplies (OM&S): The Department cannot accurately account for the value of operating material and supplies.	FY 2007	Army; Navy; Air Force; SOCOM ²	Components are implementing ERP systems that will track OM&S purchases and issuances at a transaction level to address this weakness.	FY 2017
9	Accounts Payable: The Department does not have adequate internal controls in place to provide assurance that accounts payable are recorded and properly reported in its financial reports.	FY 2004	DSS ³ ; NSA ⁴ ; Army; DLA; Air Force; Navy; SMA ⁵ ; SOCOM	Components are implementing business process changes to ensure payables are recorded upon receipt of goods or services rather than at disbursement, as well as improving capabilities to record accruals.	FY 2017
10	General Purpose Equipment: The Department does not meet Federal accounting standards for financial reporting of general personal property, specifically the financial value of general equipment.	FY 2006	Army; USACE ⁶ ; Air Force; Navy; NDU ⁷ ; MDA ⁸ ; NSA; DLA; DSS; NGA ⁹ ; OSD ¹⁰ ; USFOR-A ¹¹ ; DIA ¹² ; SOCOM	Component efforts are underway to validate existence and completeness before moving forward to record accurate valuation. A critical part of this effort is to identify property in the possession of contractors and ensure accurate information is recorded in the property system.	FY 2015
11	Financial Reporting Compilation: Due to inadequate internal management controls, the Department is unable to produce accurate Statements of Net Cost, Budgetary Resources, and Net Position, or adequately document accounting adjustments.	FY 2008	Army; USACE	The Department continues to improve business processes and controls through the implementation of ERP systems that produce accurate, timely and auditable financial reports.	FY 2015

¹ DLA: Defense Logistics Agency
² SOCOM: Special Operations Command
³ DSS: Defense Security Service
⁴ NSA: National Security Agency
⁵ SMA: Service Medical Activity
⁶ USACE: U.S. Army Corps of Engineers
⁷ NDU: National Defense University
⁸ MDA: Missile Defense Agency
⁹ NGA: National Geospatial Intelligence Agency
¹⁰ OSD: Office of the Secretary of Defense
¹¹ USFOR-A: U.S. Forces - Afghanistan
¹² DIA: Defense Intelligence Agency

	Material Weaknesses	Year Identified	DoD Components	Corrective Actions	Target Correction Date
12	Financial Reporting of Intragovernmental Eliminations: The Department is unable to collect, exchange, and reconcile buyer and seller intra-governmental transactions, resulting in adjustments that cannot be supported.	FY 2008	DCFO ¹ ; Army	The Department has developed standard business processes and data to capture trading partner information at the transaction level and to support eliminations.	FY 2014

¹ DCFO: Deputy Chief Financial Office, Office of the Under Secretary of Defense (Comptroller)

2. FMFIA Section 2, Nonfinancial Operations Material Weaknesses. The Department’s 36 Component heads utilize an entity-wide, risk-based self assessment approach to establish and assess internal management controls for nonfinancial, mission-essential operations.

Table 2b shows the weaknesses resulting from this assessment. In FY 2010, the Department identified six nonfinancial operations material weaknesses. Four of these material weaknesses previously were reported and were not resolved in FY 2010. The material weakness, “Certain Audits Do Not Meet Professional Standards,” was reported as resolved in FY 2009 and reopened in FY 2010. In addition to these five nonfinancial material weaknesses, the Department identified an additional weakness in FY 2010: “Personnel Resourcing, Qualifications and Training.”

Statement of Assurance: Qualified						
Nonfinancial Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
1. Personnel Resourcing, Qualifications and Training		1				1
2. Information Technology Management and Assurance	1					1
3. Personnel Security Investigations	1					1
4. Internal Controls Over Contingency Contracting	1					1
5. Contracting for Services	1					1
6. Certain Audits Do Not Meet Professional Standards*		1				1
Total Material Weaknesses Nonfinancial Operations	4	2				6

Table 2b-1 provides the description and corrective action plan for each material weakness related to internal controls over non-financial operations.

Table 2b-1 FY 2010 Internal Control Over Non-Financial Reporting Material Weaknesses (1 of 2)				
Material Weaknesses	Year Identified	DoD Components	Corrective Actions	Target Correction Date
1 Personnel Resourcing, Qualifications and Training: Several DoD Components have identified weaknesses resulting from an inability to hire, train, and retain enough qualified personnel to meet mission requirements.	FY 2008*	OSD ¹ ; DCMA ² ; USFOR-A ³ ; SOCOM ⁴	OSD requested a review of Acquisition and Procurement personnel to determine the workforce mix that meets risk assessment requirements. DCMA has increased the number of cost analysts and industrial engineers, established a Cost and Pricing Center, and plans to assess training and career competency progress of cost/price analysts. DCMA also plans to evaluate results of the FY 2010 hiring efforts upon completion of the 24-month training period. USFOR-A plans to establish policies and procedures to support logistics operations and will increase the number of logistical personnel.	FY 2014
2 Information Technology Management and Assurance: Reviews at several DoD Components indicate weaknesses in the management and assurance of the reliability and security of the information technology infrastructure.	FY 2003	ASD(NII) ⁵ ; AFRICOM ⁶ ; Navy; SOCOM; PACOM ⁷ ; NDU ⁸ ; DIA ⁹	AFRICOM plans to assess its consolidated enterprise and to develop additional requirements; engineer, implement, operate, and maintain a Joint Enterprise Network; and provide additional capabilities for the Tactical Local Area Network. The Navy plans to release policies that address deficiencies for Magnetic Hard Drive Disposals and unnecessary or unlawful collection of social security numbers. DON will also create personal information protection refresher training and reconcile remaining Common Tier Accounts.	FY 2012
<p>¹ OSD: Office of the Secretary of Defense ² DCMA: Defense Contract Management Agency ³ USFOR-A: U.S. Forces – Afghanistan ⁴ SOCOM: Special Forces Command ⁵ ASD(NII): Assistant Secretary of Defense for Networks and Integration Information ⁶ AFRICOM: United States African Command ⁷ PACOM: Pacific Command ⁸ NDU: National Defense University ⁹ Defense Intelligence Agency</p>				

Table 2b-1 FY 2010 Internal Control Over Non-Financial Reporting Material Weaknesses (2 of 2)

Material Weaknesses	Year Identified	DoD Components	Corrective Actions	Target Correction Date
<p>3¹ Personnel Security Investigations: The GAO noted in FY 2005 that the DoD Personnel Security Program is a high-risk program due to issues related to timeliness, quality, and program oversight, and monitoring of the personnel security clearance process. DSS reported issues related to the identification and integration of critical information from the Counter Intelligence Program and DSS organizational entities.</p>	FY 2003	OUSD(I) ² ; DSS ³	The Department plans to implement a DoD Adjudicator Certification Program; pilot an Automated Record Check Procedure; develop a comprehensive case management system; conduct an evaluation to project DoD-wide military and civilian investigations; and provide an assessment of annual performance and trends towards workload, related timelines and associated costs. DSS plans to establish the Joint Threat Assessment Fusion Center and will test and validate that all corrective actions have been completed.	FY 2011
<p>4 Internal Controls Over Contingency Contracting: The Army reported that the acquisition workforce was not adequately staffed, trained, structured or empowered to meet current and future in-theater contracting requirements.</p>	FY 2007	OUSD (AT&L) ⁴ ; Army; DCMA ⁵	Self-inspections and procurement management reviews will continue to validate the use of the Management Control Evaluation Checklist and compliance with internal control procedures for adequate contractor surveillance, manning and training.	FY 2014
<p>5 Contracting for Services: GAO has designated DoD contract management as a high-risk area due to a lack of guidance, planning, tracking, oversight, training and screening related to service contracts. The Army reported that because Contracting Officer's Representatives (COR) were poorly trained, justifications for services contracts were inadequate and there were improper uses of contractor labor.</p>	FY 2006	Army	The Army plans to implement revised management and oversight of service contracts, develop COR guidance, and provide additional resources for contract surveillance.	FY 2012
<p>6 Certain Audits Do Not Meet Professional Standards: A GAO audit and DCAA investigation identified widespread problems with DCAA audit quality, attributable in part to a focus on production volume at the expense of quality.</p>	FY 2009	DCAA ⁶	DCAA is developing policies and procedures for auditors and will institute peer reviews, life-cycle training, and workforce surveys.	FY 2012

¹ The Secretary of Defense Communications Office (SDCO) reported a weakness in Personnel Resourcing, Qualifications, and Training in FY 2008. In FY 2010, this weakness was elevated to a Department-wide system material weakness.

² OUSD(I): Office of the Under Secretary of Defense (Intelligence)

³ DSS: Defense Security Service

⁴ OUSD(AT&L): Office of the Under Secretary of Defense (Acquisition, Technology, and Logistics)

⁵ DCMA: Defense Contract Management Agency

⁶ DCAA: Defense Contract Audit Agency

3. FMFIA Section 4, Financial System Nonconformance Weaknesses: The Department requires financial system conformance with federal requirements and reports. The Department reported one weakness that includes a wide range of pervasive problems related to financial systems. Table 2c shows the resulting weakness.

Table 2c. Conformance with Financial Management System Requirements (FMFIA Section 4)							
Statement of Assurance: No Assurance							
System Nonconformance	Ref Table 1	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
1. Financial Management Systems	9	1					1
Total System Conformance Material Weaknesses		1					1

Table 2c-1, below, provides the description and corrective action plan for the material weakness related to internal controls over financial systems.

TABLE 2c-1 FY 2010 Internal Controls Over Financial Systems Material Weakness					
	Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Date
1	Financial Management Systems: Most DoD financial systems were developed decades ago to meet the requirements of budgetary accounting and do not provide the capability to record costs and assets in compliance with current accounting standards. Improvements to the current systems environment also are complicated by the use of and reliance upon many mixed (feeder) systems that are not well integrated with each other or the core financial system.	FY 2001	Army; Air Force; OSD ¹ ; DFAS ² ; DTRA ³ ; DIA ⁴ ; DLA ⁵	Most DoD Components have embarked on an effort to implement a compliant end-to-end financial management system, anchored by an enterprise resource planning (ERP) system that provides the core financial system as well as replacing many of the mixed (feeder) systems.	FY 2017
¹ Office of the Secretary of Defense ² Defense Finance and Accounting Service ³ Defense Threat Reduction Agency ⁴ Defense Intelligence Agency ⁵ Defense Logistics Agency					

Statement of Assurance over Financial Reporting, Nonfinancial Operations and Financial Systems Process:

The revised OMB Circular A-123 requires an annual Statement of Assurance that provides assurances on the effectiveness of internal controls of overall operations (non-financial program and administrative controls), the internal controls over financial reporting, and the internal controls over financial systems. The Department’s 36 Component heads are required to report their respective Component Statements of Assurance to the Secretary of Defense. The Component heads represent the 3 Military Departments, 10 Combatant Commands, Joint Staff, Office of Secretary of Defense, DoD Office of Inspector General, 19 Department Agencies, and the DoD Financial Reporting Senior Assessment Team. Following the submission of the Components’ Statements of Assurance, the Secretary of Defense produces an overall DoD Statement of Assurance that reflects the systemic material weaknesses, or material weaknesses commonly reported by the Components throughout the Department. Creating an annual Statement of Assurance includes flowcharting key business processes that impact financial reporting and non-financial operations, identifying and assessing risk within the processes, identifying internal controls, testing internal controls, establishing controls found to be deficient, and reporting on the results of the assessments and tests. The Department asserts that all Components, as prescribed by DoD’s regulatory guidelines, have reported their individual statements of assurance over internal control to the Secretary of Defense. More information concerning DoD’s process for developing the Statement of Assurance is available at <http://comptroller.defense.gov/micp.html>.

Federal Financial Management Improvement Act (FFMIA)

The DoD IG and the audit agencies within the Military Services have reported on DoD’s non-compliance with FFMIA. The DoD’s noncompliance is due to the reliance upon legacy financial management systems by the various Components. These financial systems, for the most part, do not comply with the wide range of requirements for systems compliance and therefore do not provide the necessary assurance that the core financial system or the mixed systems information can be traced to source transactional information. Table 3 reflects DoD’s compliance with FFMIA.

Table 3. Compliance with Federal Financial Management Improvement Act		
	Agency	Auditor
Overall Substantial Compliance	No	No
1. System Requirements	No	No
2. Accounting Standards	No	No
3. U.S. Standard General Ledger at Transaction Level	No	No

IMPROPER PAYMENTS INFORMATION ACT REPORTING

The Improper Payments Information Act (IPIA) of 2002, as implemented by OMB Circular No. A-123, Appendix C, "Requirements for Effective Measurement and Remediation of Improper Payments," requires federal agencies to review all programs and activities annually and identify those that may be susceptible to significant erroneous payments. On November 20, 2009, the President issued Executive Order (EO) 13520, "Reducing Improper Payments," which added several new reporting requirements for Federal agencies, including quarterly reporting of high-dollar improper payments to individuals and entities. The Improper Payments Elimination and Recovery Act (IPERA), which was passed unanimously by both houses of Congress and signed into law on July 22, 2010, is targeted at reducing wasteful spending by identifying government programs that are susceptible to significant improper payments and requiring corrective action plans be implemented to alleviate the waste. The IPERA, which amends the IPIA, established new reporting thresholds based on percentages of program outlays or dollar amounts of annual improper payments.

Based on the large volume of transactions and high dollar amounts, OMB requires the Department to report on the following programs: (1) Military Health Benefits; (2) Military Pay; (3) Civilian Pay; (4) Military Retirement; and (5) Travel Pay. The Improper Payment Reduction Outlook table, included at the end of this section, presents improper payment estimates for these programs, as well as out-year reduction targets. Commercial Pay information is included in the section entitled Recovery Auditing.

Risk Assessment

The DoD's risk assessments for each of the programs identified above address the effectiveness of internal controls in place to prevent improper payments (such as pre-payment reviews and automated business activity tools), as well as system weaknesses identified internally or by outside audit activities. The DoD's improper payment percentages are extremely low. Numerous pre- and post-payment controls further minimize and reduce improper payments.

Statistical Sampling Process

The Department uses random sampling methods designed to meet or exceed OMB's requirement to estimate annual improper payments with a 90 percent confidence interval, plus or minus 2.5 percent. For Military Pay, Civilian Pay, Military Retirement, and Travel Pay post-payment reviews performed by the Defense Finance and Accounting Service (DFAS) and the U.S. Army Corps of Engineers (USACE), the Department uses statistically valid random sampling methods. The smaller reporting Components perform a 100 percent post-payment review.

Military Health Benefits. TRICARE is a triple-option health benefit plan available to Active Duty family members, retirees and their family members, and family members of deceased service members and Reserve members under the Tricare Reserve Select program. To determine an estimate of the annual amount of improper payments, the Department uses a statistically valid sampling method for the managed-care support services contracts and the Medicare dual eligibility contractor (TRICARE Dual Eligibility Fiscal Intermediary Contract). This process takes place quarterly.

The Department samples two types of records, paid claims and denied claims, processed by the managed-care support contractors and the Medicare dual eligibility contractor.

- For the managed-care support services contracts, the Department selects the sample of paid claims from all records with government payments between \$100 to \$100,000, and audits all records with a payment of \$100,000 and over. The Department uses the same methodology to select the sample of denied payment claims. The Department stratifies both the paid and denied claims samples at multiple levels within the \$100 to \$100,000 range.
- For the Medicare dual eligibility contract, the Department reviews paid claims by sampling all records with government payments between \$1 to \$25,000, and audits all records with a government payment of \$25,000 and over. The Department selects the denied claims sample from all records with a billed amount between \$1 to \$500,000, and audits all records with billed amounts over \$500,000. The Department stratifies the paid claims sample at multiple levels within the \$1 to \$25,000 range and the denied claims sample at multiple levels within the \$1 to \$500,000 range.

Military Pay. The DFAS selects accounts for each Component to review and produce annual estimates of improper payments. The Department samples accounts for both the Active Duty (Army, Navy, Air Force, and Marine Corps) and Reserve Components (Army Reserve, Army National Guard, Navy Reserve, Air Force Reserve, Air National Guard, and Marine Corps Reserve) on a monthly basis.

Civilian Pay. Each of the Components (Army, Air Force, Navy/Marine Corps, Overseas and Defense Agencies) review sampled accounts on a monthly basis. The DFAS processes the largest portion of DoD's civilian payments; however, both the Navy and Army independently process civilian payments for civilian mariners and local national payrolls in foreign countries.

Military Retirement. The monthly random sampling universe of Military Retirement payments includes both the confirmed deceased retiree accounts and the overall population of retired and annuitant pay accounts. In FY 2011, the Department plans to expand the scope of the retired and annuitant pay reviews to include additional targeted pay entitlements that may be at risk of improper payments.

Travel Pay. The DFAS reports the largest portion of DoD's travel payments made by both the Defense Travel System (DTS) and the Windows Integrated Automated Travel System (WinIATS) for the Department of the Army. The DoD's total travel payment population includes travel payments computed, paid, and reported independently by the Military Services and other Defense agencies. The Improper Payment Reduction Outlook table, included at the end of this section, represents the combined results of the review of DFAS-disbursed travel payments, as well as for Army-Europe, Army-Korea, the Air Force, the Navy, USACE, the National Geospatial-Intelligence Agency (NGA), and the Defense Media Activity.

The DFAS sampling universe includes trip records settled and paid for each Military Service Component and the Defense Agencies through DTS, and for Temporary Duty (TDY) and Permanent Change of Station (PCS) vouchers computed and paid by DFAS for the Army through WinIATS.

Root Causes of Errors and Corrective Action Plans

Military Health. For several years, the TRICARE Management Activity (TMA) has had contract performance standards in place to ensure accurate health claims processing and payment. The annual audit process identifies overpayment amounts and projects these errors to the audit universe. Subsequently, the managed-care support contractor becomes liable for this total amount. The performance accuracy standard for this contract is no more than 2 percent in payment errors; however, the actual error rate (reported 12 months in arrears) normally falls below 1 percent. This unique contractual design, coupled with numerous pre- and post-payment controls, effectively minimizes the Government's risk for improper payments in this program.

The primary causes of military health care errors benefit payment errors are:

- Incorrect pricing (42 percent);
- Cost share/deductible errors (22 percent);
- Incorrect benefit determinations (14 percent);
- Government payment miscalculations because of other health insurance (8 percent);
- Miscellaneous (14 percent)

The TMA requires the contractor to accept the risk for making any improper payments. Historically, the error rates have been below 1 percent, with the FY 2010 actual error rate at 0.42 percent.

Military Pay. The Department projects \$505.9 million (0.61 percent of total net pay) in military pay improper payments based on review, estimates, and forecasts for October 2009 through September 2010. Approximately \$319 million (63 percent) of the total improper payments occurred within the Reserve/Guard Components. The Army Reserve and Army National Guard accounted for \$249.2 million (49 percent) of the \$505.9 million in Reserve/Guard Component improper payments.

Underpayments accounted for \$338.8 million (67 percent) of the \$505.9 million in improper payments. Most of these underpayments occurred within the Army Reserve and Army National Guard (\$207 million) and represent unpaid leave that the member did not use before discharge or de-activation back to Reserve from Active duty status. The primary reasons for the under payments:

- Leave Accountability/Lump Sum Leave (79 percent), resulting from un-reconciled/unpaid leave balances for Reservists/Guardsmen.
- Family Separation Allowance (18 percent), resulting from incorrect reporting of the entitlement.
- Basic Allowance for Housing (3 percent), resulting from incorrect reporting of the entitlement.

Eighty seven percent of the \$167.1 million in overpayments for military pay were recovered or have an action in place to recover the overpayment. In-service collections for overpayments, among select entitlement categories, amount to \$144.7 million (28.6 percent) of total military pay improper payments.

Most improper payments identified from random reviews, as well as in-service collections, are attributed to untimely or inaccurate entry into the pay systems. To rectify the causes for

payment errors, the Department continues to advise the Military Services of these results and associated reasons for the errors. The DFAS provides the Military Service financial managers with monthly reports on the results of random reviews, reasons for and dollar value of errors, and year-to-date trends.

Civilian Pay. The Department projects \$81.2 million (0.24 percent of total net pay) in total civilian pay improper payments, \$79.4 million in overpayments and \$1.6 million in underpayments. Nearly 100 percent of the overpayments identified through in-service civilian pay collections have been recovered or have an action in place to recover the overpayment. Payment errors attributed to time and attendance accounted for \$37 million of the total civilian pay in-service collections, and overseas-related civilian pay errors are estimated at \$16.8 million. The remaining payment errors were detected through random post-payment reviews and were primarily caused by time and attendance and personnel action input errors.

The primary causes of the improper payments identified from random reviews, as well as in-service collections, are untimely or inaccurate entry into the pay systems. Because most government payroll systems base their time and attendance submissions on anticipated versus actual hours worked, the Department must correct overpayments and underpayments in a subsequent pay period. Collections among the overseas civilian accounts often are attributed to repayment of overseas pay allowances that erroneously continued after the individual returned to the United States. The DFAS works diligently with the Components on corrective actions, advising them of the results of monthly civilian pay random reviews and the associated reasons for errors.

Military Retirement. Payments to deceased retirees continue to be the highest risk for improper payments in the Military Retirement program. Based on FY 2010 reviews, the Department projects approximately \$58.5 million (0.14 percent) in improper payments for this program, with almost the entire amount paid to deceased retirees. In many instances, payments to deceased retirees are unavoidable due to payment cycle dates and the fact that notifying a payroll activity of the retiree's passing is unlikely to be the first action taken by the next-of-kin. A review of confirmed payments to deceased retirees in FY 2010 indicated that the Department recovered 96.3 percent of the overpayments within 60 days, demonstrating the effectiveness of controls within the retired pay system once the Department receives confirmation of a retiree's death.

The DoD's control processes to prevent, identify, and reduce overpayments to deceased retirees include a series of periodic eligibility notifications, early detection data mining efforts, and partnerships with other Federal and state entities. The Department takes a proactive approach, routinely comparing retired and annuity payroll master file databases with the Social Security Administration's deceased records and periodically comparing records with the Office of Personnel Management's deceased files. The Department also compares its files with the Department of Veterans Affairs' cemetery database and with individual states with sizable retiree and annuitant populations (e.g., Texas, California, and Florida). If a retiree is identified through this process as being deceased, an additional validation step is required or the account is suspended from further payment. The DoD's expanded definition of "acceptable source documents for notice of death" allows DFAS to initiate reclamation actions earlier, thereby increasing recovery of funds paid after date of death.

Travel Pay. The FY 2010 projected improper payments in DTS and rates for both DTS (1.6 percent) and WinIATS (5.4 percent) reflect slight increases from the FY 2009 estimates. The FY 2010 improper payment estimates include random reviews of DTS trip records for the Military Services as well as monthly random reviews of WinIATS TDY and military PCS vouchers computed and disbursed by DFAS.

The primary reasons for DTS improper payments include:

- **Lodging (43 percent):** The Department reimbursed lodging expense without a receipt or based on an invalid receipt. The Department reimbursed lodging at the full rate when it should have reduced the payment to reflect actual cost, including when there was no cost incurred for the lodging. The traveler claimed lodging under both the “lodging” and “reimbursable expense” categories, resulting in a duplicate reimbursement.
- **Airfare (15 percent):** The Department did not pay for airfare in accordance with the receipt or did not pay airfare at all. The Department reimbursed the traveler without supporting documentation and the travel card issuing bank could not verify the transaction.
- **Rental Car (15 percent):** The Department reimbursed the rental car expense without a receipt or based on an invalid receipt. The traveler did not adjust the original cost estimate of the rental car to reflect the actual cost. The traveler claimed rental car expense under both the “transportation” and the “reimbursable expense” categories, resulting in a duplicate reimbursement.

The other causes (27 percent) of DTS errors fall into several miscellaneous categories.

Errors in the traveler’s request and Approving Official (AO) oversight resulted in nearly all of the monetary errors detected during the random reviews. On a quarterly basis, the DFAS provides the Defense Travel Management Office (DTMO) and DoD Components with error trend reports. The DFAS post-payment review personnel give presentations at Defense Travel Administrators training conferences and also brief senior service executives on these post-payment review statistics, trends, and illustrations of input errors. In addition, any improper payments identified are forwarded to the appropriate Debt Management Monitor for debt establishment and recovery.

The primary reasons for WinIATS improper payments:

- **Per Diem (37 percent):** Per diem/Meals & Incidental Expenses (M&IE) was paid at the incorrect rate, while the traveler was in leave status, and/or the traveler was paid advance per diem when it was not authorized.
- **Missing/Invalid Orders (9 percent):** The Department reimbursed the claim without TDY and PCS orders or based on invalid orders.
- **Lodging (2 percent):** The Department reimbursed lodging expense without the required lodging documentation (i.e., invalid lodging receipts), the statement of government-rate non-availability is missing, incorrect per diem rates were paid, and/or lodging taxes were incorrectly paid.

The other causes (52 percent) of WinIATS errors fall into several miscellaneous categories. The Department attributes the majority of errors to processing inaccuracies at the time of settlement and travel technician input errors. The DFAS has established an extensive set of preventative and monitoring actions, including:

Department of Defense Agency Financial Report for FY 2010

- Post-payment reviewers meet monthly with travel pay operations personnel to discuss findings and preventative measures;
- Pre-payment accuracy rates are reported by travel pay operations and monitored daily;
- Implementation of travel pay examiner training programs based on post-payment review findings and recommendations;
- Linked pre-payment to post-payment checklists to identify and prevent improper payments.

Program Improper Payment Reporting

The following table summarizes DoD's improper payment reduction outlook and total program outlays (payments) from FY 2009 through FY 2013.

Improper Payment Reduction Outlook ^(Note 8)															
Program	FY 2009			FY 2010			FY 2011 Estimate			FY 2012 Estimate			FY 2013 Estimate		
	Outlays (\$ B)	IP (%)	IP (\$ M)	Outlays (\$ B)	IP (%)	IP (\$ M)	Outlays (\$ B)	IP (%)	IP (\$ M)	Outlays (\$ B)	IP (%)	IP (\$ M)	Outlays (\$ B)	IP (%)	IP (\$ M)
Military Health Benefits <i>(Note 1)</i>	\$11.7	0.42	\$49.1	\$12.5	2.0	\$249.6	\$18.9	2.0	\$378	\$20.1	2.0	\$402.4	\$21.6	2.0	\$432.9
Military Pay <i>(Note 2)</i>	\$84.60	0.48	\$406.50	\$82.5	0.61	\$505.9	\$71	0.55	\$390.5	\$71	0.53	\$377.9	\$71.3	0.50	\$356.5
Civilian Pay <i>(Note 3)</i>	\$29.40	0.32	\$94.60	\$34.0	0.27	\$81.2	\$32.3	0.26	\$84	\$32.3	0.25	\$80.8	\$32.3	0.24	\$77.5
Military Retirement <i>(Note 4)</i>	\$38.90	0.13	\$49.50	\$43.2	0.14	\$58.5	\$44.5	0.12	\$53.4	\$44.5	0.12	\$53.4	\$44.5	0.12	\$53.4
Travel Pay <i>(Notes 5, 6, 7)</i>	\$6.60	0.95	\$59.90	\$9.3	1.91	\$174.6	\$9.4	1.85	\$173.9	\$9.4	1.80	\$169.2	\$9.4	1.77	\$164

Note 1 Military Health Benefits: For FY 2009, approximate overpayments were \$13.8 million and underpayments were \$35.3 million. TMA always reported its actual improper payment dollars and percentage 12 months in arrears. Therefore, in the FY 09 AFR, only the basic 2% estimate was shown, whereas in the FY 10 AFR, the FY 09 actuals were available and included in the current year's table. Outyear projections are flatlined at 2%, as this is the contract performance standard representing worst-case scenario. Historically, the actual error rate has been less than 1%.

Note 2 Military Pay: For FY 2010, overpayments were \$167.1 million, underpayments were \$338.8 million

Note 3 Civilian Pay represents data from DFAS, Army, and Navy. FY 2010 overpayments were \$79.5 million, underpayments were \$1.6 million.

Note 4 Military Retirement: FY 2010 overpayments were \$58.2 million, underpayments were \$0.3 million.

Note 5 Travel Pay: Includes data from DFAS, Army, Navy, Air Force, USACE, NGA, and DMA. TMA is no longer required to report separately, as all TMA travel payments now are processed by DFAS.

Note 6 DFAS data represents July 2009 through June 2010 vouchers identified in FY 2010 and includes \$1.7 million in duplicate payments that occurred between March 2008 and February 2009. The Department identifies the duplicate payments through a specific process established to determine if travelers filed in both DTS and WinIATS for the same period of travel. Navy data represents Fourth quarter, 2009 through third Quarter, FY 2010. Overpayments totaled \$145.7 million and underpayments totaled \$28.9 million.

Note 7 The large increase in travel outlays for FY 2010 was due to an increase in Army-Europe's deployments. The increase was carried forward for outyear projections for this year's reporting, but may be revised based on FY 2011 activities.

Note 8 Outyear projections for Travel, Civilian Pay, and Military Pay represent input from DFAS only.

The Department established a separate, additional process to identify duplicate travel payments in DTS and WinIATS for the Army and the Defense Agencies. The Department identifies travelers who filed vouchers in both systems through use of payment and accounting data from the two travel systems stored in the Operation Data Store, along with dates of travel. Once DFAS confirms a duplicate payment, it notifies the Component of the findings and quickly establishes a collection action to recover the funds. The FY 2010 duplicate improper payments total \$1.7 million, which includes duplicates paid from March 2008 to February 2009 that were identified in the current fiscal year. The \$1.7 million is included in the total amount of improper travel payments reported in the preceding table.

Recovery Auditing Reporting

The Department utilizes a number of different mechanisms to prevent, identify, collect, and report improper payments. Regulatory requirements regarding agency recovery auditing programs state the importance of having a cost-effective program of internal control to prevent, detect, and recover overpayments to contractors resulting from payment errors.

The Department's pre-payment controls include:

- All relevant documents are available before making payment (e.g. invoice, packing list, receiving report, inspection report);
- Payment of only the original invoice;
- Performance of recovery audits.

The Department conducts manual reviews of payment documentation at various steps in the pre-payment process. For example, the Department ensures it meets all Certifying Officer Legislation requirements prior to payment certification, to include receipt of proper documentation. In addition, before disbursement the Department performs various pre-validation checks, such as verification of payment amounts, payment type, etc. The Department currently uses the Business Activity Monitoring (BAM) tool, initially deployed in August 2008, to identify and prevent improper payments in DoD's four largest commercial payment systems, which include the Mechanization of Contract Administrative Services (MOCAS), Computerized Accounts Payable System-Windows (CAPS-Windows), Integrated Accounts Payable System (IAPS), and OnePay. These systems account for an estimated 85 percent of all Defense commercial payments. These types of preventative (vs. detective) program integrity activities consistently prove to be the most cost effective.

The DFAS also identifies improper commercial payments based on overpayments made from previous invoices detected in the current pay cycle, overpayments discovered during the contract reconciliation process, and payments made to the incorrect vendor. Further, the Department captures these improper payments in either the Contractor Debt System (CDS) or Improper Payment On-Line Database (IPOD) to identify, track, recover, and analyze to determine the root cause(s) of the improper payment.

To further ensure proper identification and recovery of improper commercial payments, the Department uses various post-payment initiatives, including periodic duplicate payment reviews performed by the DFAS Internal Review Directorate for the four major commercial payment systems. The DFAS Internal Review (IR) auditors analyze monthly extracts of invoice and disbursing data for payments made through these systems and perform various quality control

checks to ensure the data is consistent and reasonable to volume and frequency. The DFAS IR auditors identify groups they believe to be duplicate payments and refer these to DFAS Accounts Payable staff for final determination. The DFAS Accounts Payable staff updates IPOD with the agreed-upon determination and follows up to ensure DoD recoups all outstanding duplicate payments.

The Defense Logistics Agency (DLA) hired an external contractor that began conducting post-payment recovery audits in April 2009. This firm has identified approximately \$1.7 million in improper payments, and recovery efforts recently have been initiated. The DFAS now makes all of DLA's payments; however, the figures shown in the following table, entitled "FY 2010 Recovery Audit Activity," represent disbursements from DLA's legacy system.

Prior to FY 2010, TMA recovered approximately \$34.5 million out of approximately \$47.5 million in cumulative amounts identified. The majority of these recoveries were accomplished several years ago, when a private sector firm performed recovery auditing on amended Medicare cost reports. The Defense Contract Audit Agency has performed the recovery auditing function for TMA since FY 2008 and has recovered approximately \$6 million through FY 2009. The Department will report FY 2010 recoveries in the FY 2011 Annual Financial Report once the final audits are completed (TMA reports 12 months in arrears for all payments made outside of DFAS).

In FY 2010, the USACE identified \$4.1 million in improper payments and recovered all but \$30,000 thus far, representing a 99 percent recovery rate.

Department of Defense Agency Financial Report for FY 2010

FY 2010 Recovery Audit Activity (Note 1,5,6)					
Reporting Categories	DFAS (Note 2)	USACE	ARMY	DLA (Note 3)	TOTALS (Note 4)
Amount Subject to Review for Current Year Reporting	\$ 384,123,184,671	\$26,694,071,778	\$94,833,389	\$26,553,907,970	\$ 410,912,089,838
Actual Amount Reviewed and Reported - CY	\$ 384,123,184,671	\$26,694,071,778	\$67,867,930	\$2,984,126,054	\$ 410,885,124,379
Overpayment Amounts Identified for Recovery - CY	\$ 339,562,492	\$4,092,110	\$81,181	\$1,737,198	\$ 343,735,783
Amounts Recovered - CY	\$ 294,392,830	\$4,061,331	\$55,001	\$46,999	\$ 298,509,162
Overpayment Amounts Identified for Recovery - Prior Years (PYs)	\$ 213,465,364	\$34,848,647	483	\$0	\$ 248,314,494
Amounts Recovered PYs	\$ 142,727,026	\$34,325,917	483	\$0	\$ 177,053,426
Cumulative Amounts Identified for Recovery (CY+PYs)	\$ 553,027,856	\$38,940,757	\$81,664	\$1,737,198	\$ 592,050,277
Cumulative Amounts Recovered (CY+PYs)	\$ 437,119,856	\$38,387,248	\$55,484	\$46,999	\$ 475,562,588
Internal Costs	\$ 7,468,367	\$672,749		\$43,617	\$ 8,184,733
Recovery Rate	79%	99%	68%	2.7%	80%
<p>Note 1: The figures reflected in the FY 2009 AFR Recovery Auditing Chart were incorrect, as updates arrived too late for inclusion in last year's AFR. The Amounts Identified for Recovery (CY 2009) should have been \$47.1M not \$94M. In addition, the DFAS data contained in the chart for FY 2009 was through July 2009, not September 2009.</p> <p>Note 2: Data represent MOCAS and Vendor Pay disbursements.</p> <p>Note 3: The \$26.6B subject to review represents total payments processed through DLA's legacy system (SAMMS) for FY 2005-2007. These amounts were disbursed through MOCAS and therefore are not included in the chart totals to prevent possible duplication.</p> <p>Note 4: Totals (except for internal costs) include small amounts reported by Army Europe and Korea.</p> <p>Note 5: Navy commercial payments now are disbursed through DFAS and so no longer are reported separately.</p> <p>Note 6: TRICARE Management Activity reports \$31.8M in recoveries out of \$47.5M in overpayments identified from FY 2004-2009. FY 2010 actual results will be available for reporting in the FY 2011 AFR for TMA.</p>					

Business Activity Monitoring (BAM)

The DFAS utilizes the Business Activity Monitoring (BAM) tool to perform continuous, automated analysis of transactions. BAM is a software tool that provides transaction review using computer logic and algorithms to detect and prevent improper payments. The financial transactions are assembled from various source systems and then subjected to forensic financial logic and comparison.

The DFAS uses BAM to review the four largest DoD entitlement systems (MOCAS, CAPS-Windows, IAPS, and OnePay), which ensures review of 85 percent of all contract and vendor payments made by DFAS.

The BAM process facilitates rich metrics collection, which allows DFAS to focus on prevention and elimination of erroneous payments. Metrics collected in the Improper Payments BAM process in FY 2009 fueled Lean6 projects, which resulted in BAM logic changes to increase detection, system change requests for entitlement source systems, and improvements in operational business processes.

Accountability

Certifying officer legislation holds certifying and disbursing officers accountable for government funds. In accordance with 10 U.S.C. 2773a, pecuniary liability attaches automatically when there is a fiscal irregularity, i.e., (1) a physical loss of cash, vouchers, negotiable instruments, or supporting documents, or (2) an improper payment. Efforts to recover from a recipient must be undertaken in accordance with the debt collection procedures, as outlined in the DoD Financial Management Regulation Volume 5, Chapters 28 and 29, and Volume 10, Chapter 18.

Infrastructure

The Department has much of the information and infrastructure needed to reduce improper payments in each of the five improper payment program areas as well as the area of commercial pay. The DoD has implemented the BAM tool to identify potential improper commercial payments prior to disbursement. With the additional requirements for tracking and reporting payment errors that were issued during FY 2010, such as Executive Order 13520, "Reducing Improper Payments," the enactment of the Improper Payments Elimination and Recovery Act, the Payment Recapture Audit memorandum, and the Do Not Pay List, DoD will reevaluate and prioritize its resource allocations to ensure maximum compliance.

Barriers

The barrier that existed for Military Retirement in prior annual reporting has been eliminated. Under the authority of Section 324 of the 2008 National Defense Authorization Act, DFAS was able to migrate the management and operation of Retired and Annuitant Pay back to the Federal sector. This change is expected to generate more flexibility, equal or better customer service, and \$20 million to \$23 million in savings over 10 years. Conversion back to the DFAS was completed during FY 2010.