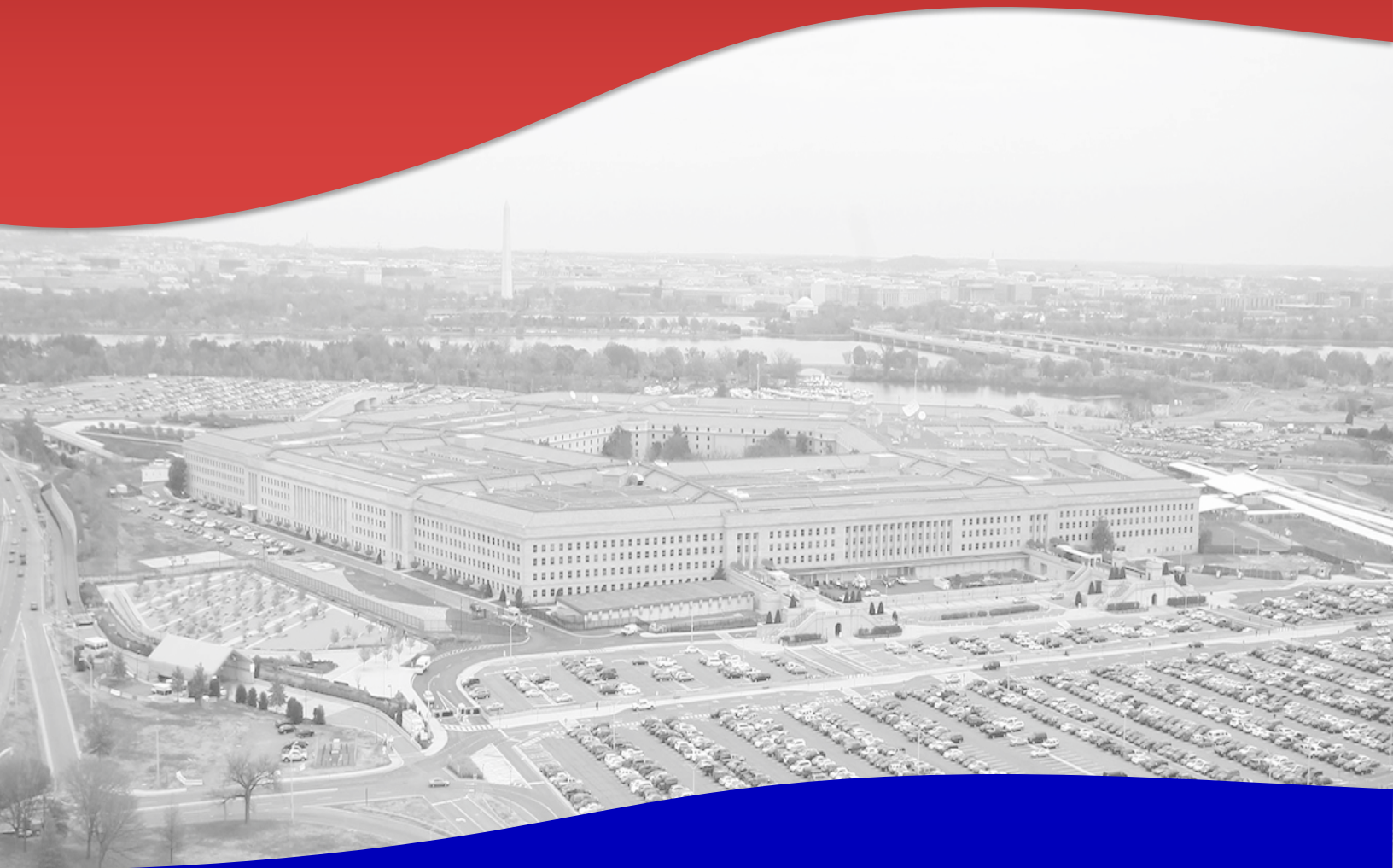# UNITED STATES DEPARTMENT OF DEFENSE

AGENCY FINANCIAL REPORT

FISCAL YEAR 2017

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SUMMARY OF FINANCIAL STATEMENT AUDIT AND MANAGEMENT ASSURANCE

The Department of Defense (DoD) management has a fundamental responsibility to develop and maintain effective internal controls to ensure that its programs operate and federal resources are used efficiently and effectively to achieve desired objectives. As discussed in the Enterprise Resource Management and Internal Controls Program subsection of the Management's Discussion and Analysis, managers throughout the Department are accountable for ensuring effective internal controls in their areas of responsibility. All DoD Components are required to establish and assess internal controls for financial reporting, mission-essential operations, and financial management systems.

Management-identified weaknesses are determined by assessing internal controls, as required by the Federal Managers' Financial Integrity Act of 1982 (*FMFIA*), the Federal Financial Management Improvement Act of 1996 (*FFMIA*), and Office of Management and Budget (OMB) *Circular No. A-123*, and fall into one of the following categories:

- FMFIA Section 2, Effectiveness of Internal Control over Financial Reporting (see Table 2a);
- FMFIA Section 2, Effectiveness of Internal Control over Operations (see Table 2b);
- FMFIA Section 4, Compliance with Federal Financial Management System Requirements (see Table 2c); or
- FFMIA Section 803(a), Implementation of Federal Financial Management Improvements (see Table 3).

Navy Sailors enter a burning building for Firefighter 1 live fire testing at Southside Regional Fire Academy.

Photo by Mass Communication Specialist 3rd Class Jonathan Clay

Summary of Financial Statement Audit

Table 1 lists the 13 areas of material weakness in the Department's financial statement reporting as identified by the DoD Inspector General (IG) in their auditor's report. In order to support the efficient use of resources in conducting audits, section 1008 of the National Defense Authorization Act *(NDAA) for FY 2002* requires that the IG limit the performance of audit procedures to be consistent with the representations of reliability made by DoD management. As such, the DoD IG will not test remediation of these material weaknesses until DoD management has represented that they have been remediated.

Table 1. Summary of Financial Statement Audit					
Audit Opinion: Disclaimer					
Restatement: Yes					
Areas of Material Weakness	**Beginning Balance**	**New**	**Resolved**	**Consolidated**	**Ending Balance**
1 Accounts Payable[1]	1				1
2 Accounting Entries[2]	1				1
3 Environmental Liabilities	1				1
4 Government Property in Possession of Contractors	1				1
5 Intragovernmental Eliminations[2]	1				1
6 Operating Materials and Supplies	1				1
7 Reconciliation of Net Cost of Operations to Budget[2]	1				1
8 Statement of Net Cost[2]	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**				**13**

The material weaknesses areas identified by the IG and presented in Table 1 differ from those identified by DoD management and presented in Table 2 for two main reasons: 1) DoD management reassessed and deemed Accounts Receivable to no longer be a material weakness and 2) DoD management defines material weakness areas using the "assessable unit" categories used in the Department's internal control program (see the footnotes to Table 1).

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[1] Material weakness area includes the following FY 2017 DoD management-identified material weakness areas listed in Table 2: Contract Vendor Pay, Reimbursable Work Orders (budgetary), Transportation of Things, Healthcare Liabilities, and Military Pay.
[2] Material weakness areas correspond to the FY 2017 DoD management-identified material weakness area Financial Reporting Compilation listed in Table 2.

Summary of Management Assurances

FMFIA Section 2, Effectiveness of Internal Control over Financial Reporting

Under the oversight of the DoD Financial Improvement Audit Readiness (FIAR) Governance Board, discussed in the *FIAR Plan Status Report*, the Department's assessment of the effectiveness of its internal controls over financial reporting identified 40 material weaknesses in FY 2017.

Table 2 lists the material weaknesses in internal controls over financial reporting, captured by end-to-end process and the assessable unit for the material weakness, and incorporates changes from the weaknesses reported in the *FY 2016 Agency Financial Report*.

A Marine with the Maritime Raid Force, 11th Marine Expeditionary Unit, jumps out of a CH-53E Super Stallion during helocast training conducted near the USS Makin Island (LHD 8) while afloat in the Indian Ocean. Helocasting allows an amphibious force to use an aircraft to travel long distances and then insert into a body of water where the unit can continue to an objective, often times using Combat Rubber Raiding Crafts.

Photo by Cpl. Devan K. Gowans

Table 2. Effectiveness of Internal Control over Financial Reporting (FMFIA Section 2)

Statement of Assurance: No Assurance

End-to-End Process	Areas of Material Weakness	FY 2016 Ending Balance	FY 2017 Revised Beginning Balance[3]	New	Resolved	Reassessed	FY 2017 Ending Balance
Budget-to-Report	Fund Balance with Treasury (FBWT)	3	3				3
	Financial Reporting Compilation	6	6				6
Hire-to-Retire	Health Care Liabilities	2	2				2
	Civilian Pay[4]	2	2			(2)	0
	Military Pay	4	4		(1)[5]		3
Order-to-Cash	Accounts Receivable - Public[6]	1	1			(1)	0
Procure-to-Pay	Contract/Vendor Pay	7	6				6
	Reimbursable Work Orders (Budgetary)	3	3				3
	Transportation of Things	2	2				2
Acquire-to-Retire	Equipment Assets	2	2				2
	Real Property Assets[7]	2	2			(1)	1
	Environmental Liabilities[8]	2	2			(1)	1
	Accountability and Management Property Furnished to Contractors for the Performance of a Contract[9]	1	1				1
	Internal Use Software (IUS)	1	1				1
Plan-to-Stock	Inventory	4	4				4
	Operating Materials & Supplies (OM&S)	3	3				3
	Requisitioning Process (Customer Orders)[10]	1	1	2	(1)[11]		2
Total Financial Reporting Material Weaknesses		**46**	**45**	**2**	**(2)**	**(5)**	**40**

[3] In FY 2016, Contract/Vendor Pay was incorrectly calculated as a total of seven weaknesses. The FY 2017 revised beginning balance was updated to reflect the correction.

[4] In FY 2017, Civilian Pay was reassessed and is no longer reported as a Department-wide area of material weakness.

[5] In FY 2017, the weakness in Military Pay related to the reconciliations between the Defense Joint Military Pay System (DJMS) and the general ledger was resolved.

[6] In FY 2017 Accounts Receivable - Public was reassessed and is no longer reported as a Department-wide area of material weakness.

[7] In FY 2017 the descriptions for Real Property Assets was consolidated into one overarching area as the material weaknesses addressed similar challenges.

[8] In FY 2017 the descriptions for Environmental Liabilities was consolidated into one overarching area as the material weaknesses addressed similar challenges.

[9] Government Furnished Property was revised to Accountability and Management Property Furnished to Contractors for the Performance of a Contract.

[10] Military Standard Requisitioning and Issue Procedures (Requisitioning Procedures) was revised to Requisitioning Process (Customer Orders).

[11] In FY 2017, the weakness in Military Standard Requisitioning and Issue Procedures (Requisitioning Procedures) related to the reconciliations of bulk obligations to transaction-level detail was resolved.

Table 2a provides a brief description of each DoD management-identified material weakness in financial reporting, with corrective actions and the target correction year.

Table 2a. FY 2017 Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)				
Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
1 Fund Balance with Treasury • Ineffective processes and controls to reconcile transactions posted to the Department's Fund Balance with Treasury (FBWT) accounts with the Treasury's records. • Collections and disbursements are reported to Treasury but are not recorded in the Department's general ledger. • Ineffective processes for providing sufficient and accurate documentation to support FBWT transactions and reconciling items.	FY 2005	Department – wide	• Track and reconcile collection/disbursement activity from the core financial systems and associated feeder systems to the Department's general ledgers and to Treasury accounts. • Develop an auditable FBWT reconciliation process, to include implementation of internal controls that ensure reconciling differences are resolved in a timely and accurate manner. • Analyze and resolve transactions posted to budget clearing accounts ("suspense" accounts). • Analyze and resolve transactions reported on Treasury's Statement of Differences (e.g., deposit in-transit, Intra-Governmental Payment and Collection, and check issue differences). • Perform aging analysis and apply reconciliations back to at least FY 2013. • Perform Statement on Standards for Attestation Engagements (SSAE) 16/ SSAE 18, Reporting on Controls on Fund Balance with Treasury – Transaction Distribution which includes Defense Cash Accountability Systems.	FY 2019
2 Financial Reporting Compilation • Ineffectively designed processes and controls to prepare accurate financial statements supported by general ledger balances that align with Department strategic and performance plans and to ensure compliance with Generally Accepted Accounting Principles and the DoD Financial Management Regulation. • Inability to reconcile detail-level transactions with the general ledgers and to provide adequate supporting documentation for adjustment entries.	FY 2007	Department – wide	• Implement a Standard Financial Information Structure (SFIS) to standardize financial reporting that aligns with the Department's mission. • Implement controls that ensure adequate documentation exists to validate and support journal entries. • Obtain population of feeder system data transactions and perform reconciliations from feeder systems to the financial statements. • Implement strategy for obtaining, reconciling and securely storing sensitive data. • Implement G-Invoicing, to include system change request requirements.	FY 2022

Table 2a. FY 2017 Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)					
	Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
	• Accounting balances are unsupported due to inadequate financial management systems and related processes and procedures. • Inconsistency between documented processes and procedures for performing reconciliations and resolving differences and the actual processes in practice. • Lack of developed approach for performing reconciliations and retaining data for sensitive activities. • Inconsistent procedures for recording Journal Vouchers and Standard Business Transactions and supporting documentation retention procedures poses a significant risk to producing accurate and complete financial statements and reports.			• Implement the SFIS Standard Line of Accounting tools to validate financial data quality and to build and implement accounting system interfaces.	
3	Health Care Liabilities • Insufficient financial reporting and accounting for all health care costs and the lack of processes to reconcile Medical Expense and Performance Reporting System data. • Inability to obtain sufficient documentation from compliant transaction-based accounting systems to support the costs of direct care provided by DoD-managed military treatment facilities.	FY 2003	Department – wide	• Develop and implement methodology for patient itemized bills to address the auditor-identified weakness related to direct care. Itemized patient bills for all patients provided care will be attainable with the deployment of the new Electronic Health Record scheduled for full deployment across the Military Health Services by close of FY 2022.	FY 2022
4	Military Pay • Ineffective processes and controls to record military pay transactions and personnel actions in a timely, complete, and accurate manner. • Unreliable and/or lack of supporting documentation for personnel actions. • Outdated military pay and financial management information technology systems lack modern capabilities to support required auditability framework. Current deficiencies require unsustainable manual activities to support auditability.	FY 2011	Department – wide	• Develop and implement a plan for an integrated pay and personnel system designed to determine pay and entitlements, report ad hoc financial management data, and capture and store key supporting documentation.	FY 2020

Table 2a. FY 2017 Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)				
Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
5 Contract/Vendor Pay • Lack of standard data structure governing purchase request format prevents traceability and use of electronic transactions from initiation of funding through contract execution. • Need to implement standard processes for recording contract obligations electronically in financial systems. • Insufficient policies governing the recording of accruals related to contracts. • Inability to reconcile contract data to financial data. Unable to reconcile buyer and seller intragovernmental and intergovernmental transactions. • Current environment does not enable match of award to accounting data for public transparency, (e.g., Data Act). • Lack of timely contract closeout and de-obligation of funds limits Department's access to capital.	FY 2003	Department – wide	• Establish and publish DoD Instruction setting policies, procedures, and data standards for purchase requests. • Develop and implement automated pre-award funds validation to ensure accounting systems can accurately record proposed contract award structure. • Scorecard all accounting and entitlement systems to track progress toward compliance with standard procedures. • Design and implement controls to ensure contract data can be accurately matched to recorded accounting data for public posting. • Develop department-wide contract closeout standard operating procedures to ensure financial systems are in balance and deobligation of funds occur, returning available funds back to programs in a timely manner. • Expand the use of accrual recording based on Wide Area Work Flow acceptance data to additional accounting systems. • Develop policies, procedures, and data standards for electronic intergovernmental/intragovernmental transactions. Pilot capability to obtain contract source data and source documentation for reconciliations to the financial records.	FY 2025
6 Reimbursable Work Orders • Lack of evidence of performance, acknowledgement of receipt of intragovernmental goods and services, and validity of open obligations. • Inability to verify the timely and accurate collection of disbursements and validate recorded reimbursable agreements meet the time, purpose, and amount criteria. • Ineffective process to collect, exchange and reconcile buyer and seller intragovernmental transaction.	FY 2011	Department – wide	• Treasury has identified G-Invoicing as a solution to intragovernmental transaction differences and will develop an online portal for conducting Buy/Sell transactions to manage the processing and approval of general terms and conditions (GT&C) Agreements, Orders, and Invoices. • Reporting entities will perform gap analyses on key processes, build and enter GT&C's agreements in G-Invoicing system, participate in G-Invoicing training, and build orders in accordance with data standards. • Reporting entities will fund, design, and build all accounting system interfaces in alignment with Treasury's G-Invoicing release schedule. • Reporting entities and the Defense Finance and Accounting Service will implement training, guidance, and management oversight related to Tri-Annual Reviews and identify and implement standard enterprise reconciliations that provide for validation of the	FY 2022

Table 2a. FY 2017 Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)					
	Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
				seller/buyer-side balances and input of supported journal vouchers for timing differences.	
7	Transportation of Things • Effective controls are not in place to prevent unauthorized use of Transportation Account Codes or unauthorized shipments from occurring. • The Department does not have a centralized process to capture, retain, and retrieve transportation documentation required to support Transportation of Things (ToT) transactions, management evaluation, and future examinations/audits. • The DoD Components lack sufficient evidence of transportation services rendered to support payment to Transportation Service Providers.	FY 2014	Department – wide	• Develop controls, processes, policies and procedures for ToT. • Continue to identify and implement standard systems and processes across the transportation community for Third Party Payment System Freight, Defense Personal Property Program, and Transportation Working Capital Fund. • Develop controls, policies, regulation, and procedures that identifies evidential matter sufficient to evidence transportation services rendered.	FY 2019
8	Equipment Assets • Ineffective processes and controls to account for the quantity and value of military and general equipment. • Insufficient internal controls and supporting documentation requirements to ensure timely recording, relief and accuracy of Construction in Progress (CIP).	FY 2006	Department – wide	• Coordinate with the Federal Accounting Standards Advisory Board to develop a Technical Release for the implementation of the Statement of Federal Financial Accounting Standards 50 guidance to establish the opening balance for Property Plant & Equipment. • Develop and implement an approach for valuing equipment and sustaining these values (including CIP) in accordance with Generally Accepted Accounting Principles, as well as modifying their Accountable Property System of Records (APSR) to ensure they capture the required data. • Develop policy guidance and update the DoD Financial Management Regulation chapters for accounting for military and general equipment, as required. • Validate asset listings and document process and control environments. • Apply controls and procedures to manage property accountability, including adequate documentation to support acquisition and disposal processes throughout the year. • Report quarterly on progress in establishing accountable records for all capitalized equipment. • Continue to convene the General Equipment (GE) Working Group to highlight policy and guidance gaps impacting the valuation of	FY 2022

Table 2a. FY 2017 Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)				
Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
			General Equipment and using the GE Working Group as a forum for sharing lessons learned. • Implement revised DoD Instruction 5000.64 that addresses internal control improvements over property accountability such as designating a Component Property Lead, annually assessing APSR capabilities, new guidance for transfers and new guidance for "non-fielded" property.	
9 Real Property Assets • Real property processes, controls and supporting documentation do not substantiate that (1) all existing assets are recorded in an accountable system of record (APSR), (2) all assets recorded in the APSR properly reflect DoD's legal interest in the asset, (3) all assets are properly valued and, (4) all assets are appropriately presented and consistently reported in the financial statements. DoD has insufficient internal controls and supporting documentation to ensure timely recording, relief and accuracy of Construction in Progress (CIP) and for real property construction or improvements.	FY 2000	Department – wide	• Implement and regularly conduct a lifecycle process for a real property physical inventory o Include validation of information for those data elements required in the calculation of Plant Replacement Value for alternative valuation in accordance with Statement of Federal Financial Accounting Standards 50. • Implement lifecycle process for regular reconciliation of real property assets, to include CIP, between the APSR and the financial statements. • Ensure adequate documentation is available to support existence and completeness and placed in service dates. • Ensure adequate documentation is available to support rights and obligations for financial statement reporting, specifically real property use agreements outlining responsibilities of each party, to include but not limited to, responsibility for financial reporting. • Implement processes and controls to support DoD policies related to financial reporting of fee, leased, or real property owned by host nations at enduring locations, the reporting of land, stewardship land/heritage assets, and deferred maintenance and repair liabilities. • Complete floor-to-book and book-to-floor baseline reconciliation of real property assets with adequate documentation to support existence and completeness and rights and obligations assertions. • Document and implement go-forward processes and control environment for all lifecycle processes to include, acquisition (and CIP), inventory, reconciliation with financial statements, and disposal. • Establish systems to properly account for and value real property assets, including CIP.	FY 2019

Table 2a. FY 2017 Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)					
	Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
				• Implement periodic evaluations over the quality of real property data by making comparisons with physical assets and annual reconciliations with tenant organizations.	
10	Environmental Liabilities • Inability to provide assurance that clean-up costs for all of its ongoing, closed, and disposal operations are identified, consistently estimated, and appropriately reported. Unable to consistently report environmental liability disclosures and supporting documentation is not properly maintained and readily available for all environmental sites.	FY 2001	Department – wide	• Implement systems, processes, and controls to ensure the accuracy of environmental liabilities identification, valuation, documentation and reporting. • Continue to implement new DoD strategy for Environmental and Disposal Liabilities (E&DL), providing guidance on capturing the environmental liability universe, estimation and modeling practices for developing the cost estimates, documenting and supporting those estimates, and roll-forward procedures for ensuring that estimates are up to date. • Identify systemic issues with reporting asset-related environmental liabilities (e.g., equipment, asbestos), to fully identify the asset universe, and value the associated disposal liabilities. • Develop documentation for E&DL cost estimating models to validate estimates and centralize common documentation where feasible. • Implement systems, processes, and controls to (1) establish, maintain , and update the complete universe of E&DL, (2) identify E&DL a retain proper support for cost estimate, and (3) establish correct roll-forward procedures for ensuring that estimates are up to date.	FY 2018
11	Accountability & Management of Property Furnished to Contractors for the Performance of a Contract • Lack of guidance and training on required policies and procedures for appropriately managing property provided to contractors resulting in incomplete DoD accountability records.	FY 2011	Department – wide	• Implement electronic solutions utilizing DoD enterprise level tools such as the Invoicing, Receipt, Acceptance, and Property Transfer (iRAPT) system and Defense Logistics Management Standards to accomplish government furnished property (GFP) transactions (e.g. shipping, receiving). • Review metrics, assertion packages, and Accountable Property Systems of Record for each Component and provide analysis of progress toward accountability. • Evaluate current processes and existing contracts to ensure accountability of GFP. • Conduct working Group meetings to share lessons learned, resolve identified problems and understand current status of corrective action plans.	FY 2019

Table 2a. FY 2017 Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)				
Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
			• Continue to train Components on the GFP accountability requirements. • Leverage audit and examination results to validate corrective actions resolved the internal control problem.	
12 Internal Use Software • The Department has not properly addressed the management and financial reporting of internal use software (IUS), which is required by the Financial Management Regulation.	FY 2015	Department – wide	• Evaluate and improve business processes to comply with new accounting standard providing flexibility for DoD on reporting beginning balance of IUS assets. • Identify existing IUS systems and applications to establish accountability over IUS assets, in accordance with DoD Instruction 5000.76. • Identify and establish IUS in development projects to begin capturing IUS capital costs in accordance with Generally Accepted Accounting Principles. • Implement processes and system changes to accountable property systems of record to sustain the accounting and accountability of IUS. • Leverage audit and examination results to validate corrective actions resolved the internal control problem.	FY 2020
13 Inventory • DoD does not have sufficient policies and procedures in place to support inventory transactions and related journal vouchers (JV). • Lack of controls to provide assurance that inventory recorded in the financial statements exist and is complete. • Lack of clear audit trails to trace transactions from source documentation to the reported total dollar values on the inventory line item on the financial statements. • Material-in-transit is reported at the summary level instead of detail level and there is a lack of adequate processes and controls to assure the amount reported is correct.	FY 2005	Department – wide	• Develop methodology and inventory condition code reports to support monthly JV related to inventory, including retention of supporting documentation for all inventory transactions and related JVs. • Ensure periodic inventories and reconciliation of inventory accounts to the systems of record is performed. • Implement methodology to value inventory in the absence of historical costs (for baseline of asset inventory). • Develop and implement processes and controls to support the valuation of inventory on a "go-forward" basis. • Modify systems to account for Material-in-transit at the detailed level.	FY 2019

Table 2a. FY 2017 Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)					
	Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
14	Operating Materials & Supplies (OM&S) • Historical cost data is not maintained and therefore inventory values cannot be reported as required by Generally Accepted Accounting Principles. • Inability to perform and document annual physical inventories of OM&S and maintain clear audit trails to permit the tracing of transactions from source documentation. • Government-owned / Contractor managed and Government Furnished Material (GFM) inventories are not accounted for in DoD accountable property systems.	FY 2005	Department – wide	• Develop and document adequate business and financial processes and controls to include establishing a baseline and "go forward" approach to track inventory values for newly acquired OM&S. • Develop interim and go forward auditable solutions for Government owned/Contractor managed and GFM inventories. • Identify and document the current inventory reconciliation processes, including key controls and financial transactions.	FY 2019
15	Requisitioning Process (Customer Orders) • Insufficient controls to validate effectiveness of Visual Inter-fund System Transaction Accountability (VISTA) system functionality for Line of Accounting to inter-fund bills. • Off-line requisition systems lack interfaces with the supply and financial automated systems to ensure timely recording of obligations.	FY 2013	Department – wide	• Validate VISTA system control implementation. • Implement system interfaces based on approved Defense Logistics Management Standards for requisitioning and internal ordering. • Conduct testing to validate system interfaces.	FY 2020

FMFIA Section 2, Effectiveness of Internal Control over Operations

DoD Components use an entity-wide, risk-based, self-assessment approach to establish and assess internal controls for mission-essential operations. The material weaknesses in operational areas are categorized in separate reporting categories.

Table 2b lists the FY 2017 material weaknesses in the internal controls over operations.

Table 2b. Effectiveness of Internal Controls over Operations (FMFIA § 2)					
Statement of Assurance: Modified					
Areas of Material Weakness	FY 2017 Beginning Balance	New	Resolved	Reassessed	FY 2017 Ending Balance
Acquisition	0	2			2
Comptroller and/or Resource Management	1				1
Contract Administration	3				3
Information Technology	0	2			2
Force Readiness	2		(1)[12]		1
Personnel and/or Organizational Management	1	2	(1)[13]		2
Security	0	1			1
Support Services	0	2			2
Supply Operations	1	1		(1)[14]	1
Total Operations Material Weaknesses	**8**	**10**	**(2)**	**(1)**	**15**

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[12] USSOCOM has resolved a lack of diversity within the Special Operations forces.
[13] USAFRICOM and USEUCOM resolved inadequate maintenance of civilian workforce critical skills.
[14] GAO cited inventory management as resolved.

Table 2b-1. FY 2017 Effectiveness of Internal Controls over Operations (FMFIA § 2)					
	Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
1	Acquisition • Many DoD acquisition programs fall short of cost, schedule, and performance expectations resulting in unanticipated cost overruns, reduced buying power, and/or in some cases resulting in a delay or reduction in the capability ultimately delivered to the warfighter. • Lack of Program Executive Office Program Manager acquisition lifecycle oversight mandated by the DoD 5000 series of policies and regulations and organizational structure is non-compliant with DoD 5000 series. Lack of effective process to support mission by identifying, assessing, and providing oversight of development and procurement solutions. Inadequate documentation and filing of acquisition records.	FY 2011 FY 2017	Department – wide Defense Health Agency, Defense Threat Reduction Agency, Joint Improvised Threat Reduction Agency	• Implement DoD 5000 series policy mandates and guidance to properly align acquisition with Agency Mission and Needs which reduces risk and impacts to cost, schedule and performance. • Continue to improve implementation of Better Buying Power 3.0 and clarification of DoD Instruction 5000.02. • Develop and implement Procedural Instruction for Acquisition Approval and Governance. Create supporting tools to aid and inform decisions, reduce the staff effort to review the programs, and improve the monitoring and forecasting of potential trouble or risk areas. • Conduct Systems Reviews, Capability Portfolio Reviews, Configuration Steering Boards and Cost Reviews to identify process inefficiencies and improve the acquisition management process. • Develop additional procedures to establish oversight controls for programs, including procedures to report cost, schedule and performance variances, and to address reported variances. • Establish a system of tracking to report acquisition program performance and highlight variances.	Reassessed annually FY 2019

2	Comptroller and Resource Management
	• Ineffective internal controls and management oversight for processes such as management of improper payments and use of government travel charge cards, Internal Use Software, and property furnished to contractors.
		FY 2013	Department – wide	• Brief leadership, appoint and train staff, develop risk profiles, conduct initial, quarterly and annual validation and assessment, and automate as appropriate.
				• Implement instructions from the October 2016 DoD memorandum "Preventing Travel Pay Improper Payments and Enforcing Recovery" including:
				  o Implement sufficient controls to verify that all required receipts and substantiating documents are provided and uploaded into travel systems,
				  o Verify that claimed amounts match documents and receipts,
					FY 2018

Table 2b-1. FY 2017 Effectiveness of Internal Controls over Operations (FMFIA § 2)				
Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
			o Implement adequate segregation of duties in payment approvals, and o Maintain continuous monitoring over improper payments and take appropriate action to mitigate instances of improper payments.	
3 Contract Administration • The Department must strategically manage Services Acquisition, define outcomes, and capture data to do so. • The Department continues to face challenges meeting fiscal year competition goals and needs to address ill-suited contract arrangements and utilize incentives. • The Acquisition workforce is not appropriately sized, trained, and equipped to meet the Department's needs.	FY 2009	Department – wide	• Continue to track and monitor training requirements for Acquisition workforce including new training for Mid/High Level Requirements and Contracting Professionals. • Continue to implement the April 2016 DoD publication, "Guidance on Using Incentive and Other Contract Types" when selecting and negotiating a contract type.	Reassessed annually
4 Force Readiness • Independent and internal reviews of DoD's nuclear enterprise identified problems and recommendations needed for a safe, reliable, and credible nuclear deterrent. These included internal control related items such as a need for increased managerial oversight, for an improved self-assessment program, for increased oversight capability, and for useful nuclear inspection reports. The reviews also made recommendations to address these problems.	FY 2016	Department – wide Nuclear Enterprise	• Develop corrective action plans that align with the recommendations from the independent reviews.	Reassessed annually
5 Information Technology • DoD financial and business management systems and processes do not provide reliable, timely, accurate information.	FY 2010	Department – wide	• Expand review and analysis of proposed information technology (IT) systems. Update the DoD Instruction (DoDI) 5000.73 and increase Investment Review Board oversight. The target date to correct this material weakness coincides with the full deployment schedule of the core business systems.	FY 2020
• Systemic shortfalls in implementing cybersecurity measures to guard the data protection environment. Gaps in cybersecurity access controls including privileged user authentication and public key infrastructure and device hardening/encryption	FY 2010	Department - wide	• Establish processes to ensure stakeholder participation in the Cybersecurity Scorecard meetings and alignment of service scorecard metrics to audit findings. • Revise current user system access policy, to include clear guidance on requirements for privileged user access authorization and	Reassessed annually

Table 2b-1. FY 2017 Effectiveness of Internal Controls over Operations (FMFIA § 2)					
	Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
	contributing to data protection vulnerabilities. Issues exist in policy compliance with cybersecurity measures, oversight, and accountability.			credential revocation, user access and control training certification, user monitoring and Public Key Infrastructure-based authentication/credentials. • Revise current acquisition and IT purchase contracts and policy to require the adoption of established user access controls and encryption/hardening standards. • Revise current policy on shared file and drive protection, to include requirements for encryption use and stringent password protection that at a minimum meets password requirements specified in DoDI 8520.03 for stronger authentication.	
6	Personnel and Organizational Management • Identified high-level undesirable trends in personnel systems, processes and organization to include inefficient alignment of roles and responsibilities and organizational structure as well as a lack of comprehensive operating procedures. Insufficient standard formal training opportunities and certifications for personnel.	FY 2017	Department – wide	• Update current policy to delineate roles and responsibilities of organizations responsible for personnel and pay service delivery, auditability, and internal controls. Conduct formal training concerning new processes and instructions. • Implement process to improve personnel and pay service delivery model and integrate automated personnel and pay information system, and validate corrective action resolve internal control deficiencies.	FY 2020
	• Significant delays in adjudicating personnel matters of up to >18 months are impacting personnel morale and potentially reenlistment.	FY 2017	Department - wide	• Continue to seek manpower funding to temporarily supplement manpower resources.	FY 2018
7	Security • DoD facilities may not have sufficient trained/qualified physical security personnel and infrastructure funding resources necessary to adequately protect assets, facilities, personnel, and mission. Issues regarding policy/contract sufficiency and compliance regarding security force training and accountability are involved.	FY 2017	Department of the Navy	• Revise security personnel contracts to include clear guidance on training completion, monitoring, and documentation requirements, including weapons qualifications. • Revise current security policy to include documentation retention and training requirements. • Revise security policy to require the completion and maintenance of security plans at the regional level. • Review access to approved DoD weapons qualification facilities and opportunities, require planning requirements and ensure policy compliance enforcement and accountability.	Reassessed annually

Table 2b-1. FY 2017 Effectiveness of Internal Controls over Operations (FMFIA § 2)				
Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
8 Support Services • Insufficient Component/assessable unit (AU) audit or review of internal operations: Lack of evidence showing sufficient leadership actions regarding internal audit or review results. Excessive Government Accountability Office and DoD Inspector General (IG) findings. IG report indicates 37 percent of DoD internal audit organizations have deficiencies or fail in effectively monitoring Component/AU activities, several DoD Components/ AUs do not seem to have an internal audit/review function. Systemic deficiencies exist across the audit and review services.	FY 2005	Department – wide	• Generate requirements for internal audit/review of operations performance and law, regulation, and policy compliance and document in DoD instruction. • Generate and deliver training in audit objectives and techniques to Department leadership and entire global DoD audit/review and managements' internal control program communities. • Form Office of the Secretary of Defense-level audit function reviewing the audit performance of DoD entity audit/review functions and reporting to Department senior leadership routinely.	FY 2020
• Business Transformation: The Department spends billions of dollars each year to maintain key business functions intended to support the warfighter. Lack of support for transformation. DoD continues to confront decades-old management weaknesses related to its business functions that support these forces.	FY 2005	Department – wide	• Adopt a reorganization under the new Chief Management Officer in accordance with the National Defense Authorization Act for FY 2018. Initiate expanded Department-wide continuous process improvement (CPI) training, develop CPI experts, and promote continuous and visible leadership support for transformation.	FY 2020
9 Supply Operations • Government Accountability Office identified several Department-wide weaknesses in the areas of asset visibility and materiel distribution.	FY 2011	Department – wide	• Improve Supply Chain Management operations through better demand forecasting, asset visibility, and distribution processes. Establish executive level reform initiative to address supply chain improvement in FY 2018.	Reassessed annually

Other Information

FMFIA Section4, Compliance with Federal Financial Management System Requirements

The Department requires financial system compliance with federal requirements and reports. The Department reported one weakness that includes a wide range of pervasive problems related to financial systems.

Table 2c. Compliance with Federal Financial Management System Requirements (FMFIA § 4)					
Statement of Assurance: Systems do not conform to financial management system requirements					
Non-Conformances	FY 2017 Beginning Balance	New	Resolved	Reassessed[15]	FY 2017 Ending Balance
1. Financial Management Systems	4	0	0	(1)	3
Total System Conformance Material Weaknesses	**4**	**0**	**0**	**(1)**	**3**

Military Working Dog (MWD) unit Master-at-Arms 1st Class Stephanie M. Durazo instructs Master-at-Arms 2nd Class Karen L. Crocker at Naval Support Activity Souda Bay with military working dog Eeverest. The canines with the MWD unit are used to apprehend suspects and to detect explosives and narcotics while searching buildings, ships and submarines.

Photo by Heather Judkins

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[15] Two of the material weaknesses reported in FY 2017 related to lack of controls in place for legacy, core, and ERP (replacement) systems. One of the material weaknesses cited a lack of entity-level technology general controls, application-level general controls and automated application controls and the other cited a lack of internal controls for access, segregation of duties, configuration management, system interfaces and audit trails. These are all control domains addressed by FISCAM and have been combined into one material weakness.

Table 2c-1. FY 2017 Compliance with Federal Financial Management System Requirements (FMFIA § 4)					
	Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
1a	Financial Management Systems *Business System Modernization* • The Department has not fully defined and consistently implemented the full range of business systems modernization management controls. As a result, it may not be able to adequately ensure that its business system investments are the right solutions for addressing its business needs, as indicated by the Government Accountability Office 2015 High Risk report. *FFMIA Compliance* • The Department's financial systems currently do not provide the capability to record financial transactions in compliance with the Federal Financial Management Improvement Act of 1996 (FFMIA), current federal financial management requirements, applicable federal accounting standards, and the Treasury United States Standard General Ledger at the transaction level.	FY 2001	Department – wide	*Business Systems Modernization & FFMIA Compliance* • The Department will reduce the number of not-audit-ready information technology systems by 23 by FY 2022. • To date, a total of 20 Treasury Index (TI)-97 Other Defense Organizations (ODOs) have been migrated to a common Enterprise Resource Planning (ERP) system, the Defense Agencies Initiative (DAI), which represents 91 percent of TI-97 appropriations received. There are five additional ODOs scheduled for deployment in FY 2018 through FY 2020. The DAI application and the data center hosting location (the Defense Information Systems Agency) both received unmodified Service Organization Controls (SOC) 1 reports for FY 2017. DAI is an FFMIA compliant Oracle ERP commercial off-the-shelf solution. • With the assistance of the Joint Interoperability Test Command, the Office of the Under Secretary of Defense (Comptroller) (OUSD(C)) has completed Standard Financial Information Structure (SFIS) compliance assessments for 16 systems through FY 2017. Assessments for an additional 22 systems are currently planned through FY 2020. The SFIS requirements are aligned to and consistent with FFMIA requirements. • OUSD(C) updated the Financial Improvement and Audit Readiness (FIAR) Guidance in April 2017 to include additional guidance related to identifying relevant financial and non-financial systems and performing FFMIA assessments. System owners record the FFMIA compliance status for their applications in the FIAR Systems Database concurrent with audit readiness status.	FY 2025

Table 2c-1. FY 2017 Compliance with Federal Financial Management System Requirements (FMFIA § 4)					
	Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
1b	**Financial Management Systems** *General & Application Controls (FISCAM)* • The Department's information technology systems environment includes numerous legacy systems, core enterprise systems that support the major end-to-end processes, and nine Enterprise Resource Planning (ERP) systems. Most of the business legacy systems were designed to support functional purposes, such as human resource management, property management, and logistics management, and not originally for auditable financial statement reporting. The current systems environment is made up of many legacy, core, and newly implemented (feeder and general ledger) systems that lack integration and are not in line with the Federal Information System Controls Audit Manual (FISCAM) requirements with regards to entity-level technology general controls, application-level general controls and automated application controls (including security management, access, segregation of duties, configuration management, system interfaces, master data, and audit trails).	FY 2001	Department – wide	*General & Application Controls (FISCAM)* • In support of the bi-annual Financial Improvement and Audit Readiness (FIAR) Plan Status Report (FPSR) submitted to congress, the Office of the Under Secretary of Defense (OUSD(C)) has established a database, the FIAR Systems Database, to identify applications and hosting locations that impact DoD financial statement audits and track the auditor feedback regarding system controls reliance. As reported in the May 2017 FPSR, OUSD(C) has identified 198 applications that are relevant to financial reporting 46 of which are considered audit ready by financial statement auditors, 22 that are considered as not audit ready, and 130 that have not yet been evaluated as part of a financial statement audit. • The Military Departments continue to deploy their ERPs to all Commands along with software upgrades, implement system change requests and standup formal enterprise monitoring program for transitioning to Risk Management Framework along with moving commands off of legacy systems onto target systems. • In 2005, DoD Service Organizations began to obtain Service Organization Control (SOC) 1 Reports for systems and hosting services. For FY 2017, DoD Service Organizations have obtained 11 unmodified opinions, 5 modified opinions, and three additional SOC 1s are currently planned for FY 2017 – FY 2018. Service Organizations have also been instructed to provide plans for SOC 1 scope expansions and additional SOC 1 reports. • OUSD(C) has implemented a database to track auditor Notifications of Findings and Recommendations (NFRs) for Service Organization SOC 1 reports and associated corrective actions. Beginning in FY 2018, the NFR tracking will be extended to additional DoD entities responsible for systems that impact financial reporting.	FY 2025

FFMIA Section 803(a), Implementation of Federal Financial Management

Section 803(a) of the FFMIA requires each Federal agency to implement and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger (USSGL) at the transaction level. The DoD IG and the audit agencies within the Military Services have reported on the Department's noncompliance with FFMIA. The Department's noncompliance is due to its reliance upon legacy financial management systems by the various Components. These legacy financial systems, for the most part, do not comply with the wide range of requirements for systems compliance, in accordance with FFMIA and therefore do not provide the necessary level of assurance that the core financial system data or the mixed systems information can be traced to source transactional documentation. Table 3 reflects the Department's compliance with FFMIA.

Table 3. Compliance with Section 803(a) of the Federal Financial Management Improvement Act (FFMIA)		
	Agency	**Auditor**
1. Federal Financial Management System Requirements	Lack of Compliance Noted	Lack of Compliance Noted
2. Applicable Federal Accounting Standards	Lack of Compliance Noted	Lack of Compliance Noted
3. USSGL at Transaction Level	Lack of Compliance Noted	Lack of Compliance Noted

PAYMENT INTEGRITY

The *Federal Improper Payments Coordination Act of 2015* amended the Improper Payments Elimination and Recovery Improvement Act of 2012 (*IPERIA*) and earlier legislation[16] affecting improper payments and requires extension of Departmental reporting of its data analytics performance. The intent is to ensure federal and state entities maintain strong financial management controls to better detect, prevent, and report improper payments to the President and the Congress in the annual Agency Financial Report (AFR).

Office of Management and Budget (OMB) Circular No. A-123, *Appendix C* defines an improper payment as any payment that should not have been made or that was made in an incorrect amount under statutory, contractual, administrative, or other legally applicable requirements. Incorrect amounts are overpayments or underpayments that are made to eligible recipients (including inappropriate denials of payment or service, any payment that does not account for credit for applicable discounts, payments that are for an incorrect amount, and duplicate payments). An improper payment also includes any payment that was made to an ineligible recipient or for an ineligible good or service, or payments for goods or services not received (except for such payments authorized by law). In addition, when an agency's review is unable to discern whether a payment was proper as a result of insufficient or lack of documentation, this payment must also be considered an improper payment.

The Department of Defense (DoD) reports its improper payments and payment recapture programs in accordance with applicable laws and regulations. The following subcategories are included in this section:

   I.   Risk Assessment
  II.   Payment Reporting
        A. Root Causes
        B. Corrective Actions
 III.   Recapture of Improper Payments Reporting
 IV.   Barriers
  V.   Accountability
 VI.   Agency Information Systems and Other Infrastructure
VII.   Sampling and Estimation
VIII.   Significant Accomplishments

The Department reports improper payments for the following nine programs:

1. Military Health Benefits – payments made by the Defense Heath Agency (DHA) to private sector contractors for delivery of health care services to TRICARE eligible beneficiaries.

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[16] Improper Payments Information Act of 2002 (*IPIA*), as amended by the Improper Payments Elimination and Recovery Act of 2010 (*IPERA*) and the Improper Payments Elimination and Recovery Improvement Act of 2012 (*IPERIA*)

2. Military Pay – payments made by the Defense Finance and Accounting Service (DFAS) to active and reserve/guard service members for salary, benefits, and other compensation entitlements.

3. Civilian Pay – payments made by DFAS to civilian employees for salary, benefits, and other compensation entitlements.

4. Military Retirement – payments made by DFAS to military retirees and their surviving spouses and other family members for pension and/or disability entitlements.

5. DoD Travel Pay – payments made by DFAS, the Army, the Navy, and the Air Force to active and reserve/guard service members and civilian employees for temporary and permanent travel and/or transportation related expenses.

6. DFAS Commercial Pay – payments made by DFAS, the Army, and the Navy to vendors and contractors for goods and services.

7. Commercial Bill Pay Office Naples – payments made by the Navy overseas Naples office to vendors and contractors for goods and services.

8. USACE Travel Pay – payments made by the U.S. Army Corps of Engineers (USACE) to active and reserve/guard Service Members and civilian employees for temporary and permanent travel and/or transportation related incurred expenses.

9. USACE Commercial Pay – payments made by USACE to vendors and contractors for goods and services.

I.   Risk Assessment

In Fiscal Year (FY) 2017, the Department applied statistical sampling and estimation methods to produce and report statistically valid improper payment estimates for each of the nine programs described above. In accordance with OMB Circular No. A-123, Appendix C, agencies are not required to perform additional risk assessments on programs reporting improper payment estimates. However, any new programs identified must be assessed for improper payment risk prior to reporting an improper payment estimate.

The Navy Commercial Bill Pay Office (CBPO) Singapore, a new program, performed a risk assessment for commercial vendor payments in FY 2017 in coordination with the Department of Navy Office of Financial Operations. CBPO Singapore conducted both a quantitative and a qualitative risk assessment by using a simple random sampling plan and a questionnaire in accordance with OMB Circular No. A-123, Appendix C. The risk assessments indicated that strong internal controls are in place and the program is not susceptible to significant improper payments. However, CBPO Singapore will perform post-payment reviews and report improper payment results in FY 2018.

II.   Payment Reporting

Table 4 reports the estimated amount of payments that were improperly paid and the corresponding percent by program for FY 2017. It also reports the estimated amount of improper payments that resulted in overpayments or underpayments and the OMB approved reduction targets by program for FY 2018

USS Hopper (DDG 70) prepares to moor in Homer, Alaska, for a scheduled port visit. Hopper is visiting Homer in conjunction with its participation in Northern Edge 2017. Northern Edge is a biennial training exercise conducted in the Joint Pacific Alaska Range Complex, which is comprised of the area within the Gulf of Alaska, as well as land and airspace within the state, and includes participation from units assigned to Alaskan Command, U.S. Pacific Fleet, U.S. 3rd Fleet, Marine Corps Forces Pacific, and U.S. Army Pacific.

Photo by Mass Communication Specialist 3rd Class Joseph Montemarano

Table 4. Improper Payment Reduction Outlook													
($ in millions) 12 month Sampling Timeframe for FY 2017 data													
Program Name	FY2016 Outlays ($M)	FY2016 IP Amount ($M)	FY 2016 IP Rate	FY2017 Outlays ($M)	FY2017 IP Amount ($M)	FY 2017 IP Rate	FY2017 Over-payment $	FY2017 Under-payment $	FY2018 Est. Outlays	FY2018 Est. IP %[6]	FY2018 Est. IP $	Month and Year start date for data	Month and Year end date for data
Military Health Benefits[1, 2, 3, 4, 5, 6]	$20,461.50	$146.10	0.71%	$23,883.30	$150.17	0.63%	$128.00	$22.17	$24,862.52	1.40%	$349.23	Aug-16	Jul-17
Military Pay[7]	$114,902.75	$196.23	0.17%	$96,777.27	$182.51	0.19%	$175.60	$6.91	$81,511.01	0.20%	$163.02	Aug-16	Jul-17
Civilian Pay[7]	$58,088.10	$58.73	0.10%	$61,811.17	$68.10	0.11%	$68.10	$0.00	$65,772.87	0.10%	$65.77	Aug-16	Jul-17
Military Retirement[7]	$59,931.73	$9.46	0.02%	$60,353.93	$127.58	0.21%	$78.45	$49.13	$54,445.20	0.21%	$114.33	Aug-16	Jul-17
DoD Travel Pay[8, 9]	$6,254.67	$451.99	7.23%	$5,279.78	$263.34	4.99%	$248.64	$14.70	$7,790.60	6.00%	$467.44	Jul-16	Jun-17
DFAS Commercial Pay[10]	$248,536.45	$110.82	0.04%	$259,165.16	$0.86	0.00%	$0.16	$0.70	$260,251.35	0.04%	$103.94	Jul-16	Jun-17
Commercial Bill Pay Office Naples[11]	N/A	N/A	N/A	$570.10	$0.01	0.00%	$0.01	$0.00	$570.10	0.00%	$0.00	Jul-16	Jun-17
Navy ERP Commercial Pay[12]	$6,901.27	$0.00	0.00%	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
USACE Travel Pay[13]	$188.85	$0.38	0.20%	$196.03	$1.58	0.81%	$1.13	$0.45	$203.47	0.70%	$1.42	Jul-16	Jun-17
USACE Commercial Pay[14, 15]	$18,158.00	$0.00	0.00%	$8,945.05	$163.20	1.82%	$161.17	$2.03	$26,306.71	1.37%	$360.40	Jul-16	Dec-16
TOTAL	**$526,522.05**	**$973.71**	**0.18%**	**$516,981.79**	**$957.35**	**0.19%**	**$861.26**	**$96.09**	**$521,713.83**	**0.31%**	**$1,625.55**		

[1] Per OMB direction, the FY 2016 IP rate was revised from .74% to .71% to match information reported by OMB in FY 2016 on the paymentaccuracy.gov website. In FY 2016, DoD reported a .74% IP rate because though total outlays for DHA were $20,461.50, the IP rate was based on a total outlays number of $19,681.65, the difference resulting from 1) the TPharm quarterly May15 – Jul15 audit was not conducted due to system constraints; 2) the TPharm Oct14 – Sept15 low dollar audit was not conducted due to contractor's opposition to participate; and 3) the ADDP semi-annual Aug14 – Jan15 audit was not conducted due to system constraints.

[2] DHA reports data 12 months in arrears. DHA's audits require 10-12 months to conclude, thus this FY 2017 Agency Financial Report (AFR) includes data from FY 2016 audits.

[3] FY 2017 outlays are the sum of the dollars paid by private sector contractors (i.e., TRICARE Managed Care Support Contracts (MCSCs), TRICARE Dual Eligible Fiscal Intermediary Contract (TDEFIC), TRICARE Overseas Program (TOP), TRICARE Pharmacy Program (TPharm), and Active Duty Dental Program (ADDP)) and reviewed by an external independent contractor (EIC) on a quarterly basis. The Oct15 – Sept16 TPharm low dollar audit, representing $138,057,695 paid dollars, was not performed due to the contractor opting out of the review (with approval by the Contracting Officer Representative (COR)). Therefore, these dollars are not included in the FY 2017 outlays. In addition, the FY 2017 outlays also include Administrative payments shared among multiple contractors to administer the TRICARE program and other contracts that are not included in DHA EIC audits (i.e., Uniformed Services Family Health Plan, Women, Infants, and Children, TRICARE Dental Program, TRICARE Retiree Dental Program, and Mail Order Pharmacy), but which have internal and external pre and post-payment controls. Administrative payments are validated via TRICARE Encounter Data (TED) system program edits, COR review/validation procedures, and/or internal/external financial audits.

[4] The FY 2017 IP rate of 0.63 percent does not represent a true statistical estimate for DHA because the Oct15 – Sept16 low dollar TPharm audit was not conducted.

[5] The FY 2018 estimated outlays were calculated using the Office of Management Budget Consumer Price Index for All Urban Consumers (CPI-U) Annual Averages and Percent Change Table. As DHA reports 12 months in arrears, the FY 2017 CPI-U medical percent change was used to calculate the FY 2018 outlay estimates.

[6] DHA uses 1.75 percent as its out-year target because that is the contractual claims processing performance requirement. DHA has had contracts with payment accuracy performance standards for many years, wherein the contractor is required to meet TRICARE policy or contractual payment accuracy performance standards as a result of the quarterly or semi-annual EIC compliance reviews. While the Military Health Benefits target for FY 2018 has increased, DHA lowered the payment accuracy performance standard from 2% to 1.75% therefore DoD is confident that 1.40% is an aggressive improper payment reduction target for this program.

[7] Over the past five FYs, DoD has reported improper payment rates of less than one percent for the following programs: Civilian Pay, Military Pay, Military Retirement, and DFAS Commercial Pay. Since the rates are very low, DoD is unable to measure a statistically valid difference between the improper payment rates and the future year reduction targets for these programs. As such, DoD's FY 2018 reduction targets for these programs remain constant or flat to the FY 2017 reported IP rates.

[8] DoD Travel Pay does not include Navy WinIATS PCS/TDY payments as the Navy was not able to complete WinIATS reviews in FY 2017 due to resource constraints. Navy is actively working to complete their reviews of FY 2017 payments by Dec17 and will either file an addendum to this table or report 24 months of WinIATS data in the FY 2018 AFR. Moreover, this program includes only nine months of DFAS Defense Travel System (DTS) data (Jul16 – Mar17). Post-payment reviews were not able to be conducted on DTS vouchers created between Apr17 – Jun17 due to a catastrophic data failure by a contract provider resulting in an irrecoverable loss of supporting documentation. As a result, DoD was forced to exclude DTS travel payments between Apr17 – Jun17 from its FY 2017 sampling population. Furthermore, this program includes only eight months of USMC WinIATS data (Nov16 – Jun17). USMC is actively working to complete their reviews of FY 2017 payments and will report 16 months of WinIATS data in the FY 2018 AFR.

[9] The DoD Travel Pay reduction target for FY 2018 is being increased to six percent. The average rate for this program based on the rates reported in FYs 2015, 2016, and 2017 results in 6.7 percent. However, DoD is confident that six percent is an achievable target based on the corrective actions implemented to date to reduce travel improper payments.

[10] The DFAS Commercial Pay sampling timeframe was Jul16 – Jun17 for the majority of the commercial payment systems, and Jun16 – May17 for the Financial Accounting and Budgetary System, the Standard Voucher Examination System, and the Transportation Financial Management System. This program also includes Army OCONUS Commercial Vendor Services payments and payments from the Navy Enterprise Resource Planning (ERP) program.

[11] Per OMB direction, FY 2016 data for the Commercial Bill Pay Office (CBPO) Naples was removed since DoD did not submit a sampling plan for this program to OMB in FY 2016 and therefore, OMB did not report improper payments data for this program on the paymentaccuracy.gov website in FY 2016. Please note, DoD reported the following information for the CBPO Naples in the FY 2016 AFR: Outlays = $472.03, IP % = 0.01%, IP = $0.06.

[12] Effective FY 2017, the Navy ERP Commercial Pay program was sampled by DFAS, and is reported as part of the DFAS Commercial Pay program.

[13] The FY 2018 estimated IP rate for Travel Pay equals the FY 2017 IP rate minus the difference of the FY 2017 IP rate minus the FY 2016 IP rate multiplied by 25 percent.

[14] Due to implementation of revised sampling plan USACE was unable to complete a 12-month review of FY 2017 data for Commercial Pay. Commercial Pay FY 2017 outlays equal only the first two quarters in the sampling timeframe. Six quarters will be reported in the FY 2018 AFR.

[15] The FY 2018 estimated IP rate for Commercial Pay equals the FY 2017 IP rate minus the difference of the FY 2017 IP rate minus the FY 2016 IP rate multiplied by 25 percent.

Table 5 reports the amount of improper payments identified in samples by program that resulted in actual monetary losses to the government. The purpose of this classification is to estimate the monetary loss to the Federal Government due to improper payments. Monetary loss to the Government would be an amount that must not have been paid and in theory should/could be recovered. This table excludes improper payments resulting from insufficient supporting documentation.

Table 5: Improper Payment Classification		
($ in millions)		
Program or Activity	Actual Monetary loss to the Government identified in Sample	Estimated Total Monetary loss to the Government
Military Health Benefits	$ 4.00	$ 74.05
Military Pay	$ 174.24	$ 175.60
Civilian Pay	$ 68.10	$ 68.10
Military Retirement	$ 8.52	$ 78.44
DoD Travel Pay	$ 3.15	$ 151.28
DFAS Commercial Pay	$ 0.00	$ 0.16
Commercial Bill Pay Office Naples	$ -	$ -
USACE Travel Pay	$ 0.01	$ 1.13
USACE Commercial Pay	$ -	$ -
TOTAL	$ 258.03	$ 548.76

Table 6 reports the root cause for overpayments and underpayments by amount and by program for FY 2017.

Table 6: Improper Payment Root Cause Category Matrix

($ in millions)

Program Name	Payment Type	Inability to Authenticate Eligibility	Administrative or Process Errors Made by: Federal Agency	Administrative or Process Errors Made by: State or Local Agency	Medical Necessity	Insufficient Documentation to Determine	Notification of death after monthly payments disbursed for Military Retirees and Annuitants	Other reason (1): Authorization/ Preauthorization Needed	Other reason (2): Development Required	Other reason (3): OHI Payment Omitted	Other reason (4): DRG Reimbursement Error	Other reason (5): Timely Filing Error	Other reason (6): Other	TOTAL
Military Health Benefits	Overpayments	$ 0.01	$ 49.69	$ -	$ 1.57	$ 61.54	$ -	$ 4.66	$ 0.20	$ 2.58	$ 0.48	$ 0.01	$ 7.26	$ 128.00
Military Health Benefits	Underpayments	$ 0.56	$ 19.14	$ -	$ -	$ -	$ -	$ 0.38	$ -	$ 0.31	$ 1.44	$ 0.05	$ 0.29	$ 22.17
Military Pay	Overpayments		$ 175.60											$ 175.60
Military Pay	Underpayments		$ 6.91											$ 6.91
Civilian Pay	Overpayments		$ 68.10											$ 68.10
Civilian Pay	Underpayments		$ -											$ -
Military Retirement	Overpayments		$ 70.35				$ 8.10							$ 78.45
Military Retirement	Underpayments		$ 49.13											$ 49.13
DoD Travel Pay	Overpayments		$ 110.30			$ 138.34								$ 248.64
DoD Travel Pay	Underpayments		$ 14.70			$ -								$ 14.70
DFAS Commercial Pay	Overpayments		$ 0.16											$ 0.16
DFAS Commercial Pay	Underpayments		$ 0.70											$ 0.70
Commercial Bill Pay Office Naples	Overpayments		$ 0.01											$ 0.01
Commercial Bill Pay Office Naples	Underpayments		$ -											$ -
USACE Travel Pay	Overpayments			$ 1.13										$ 1.13
USACE Travel Pay	Underpayments			$ 0.45										$ 0.45
USACE Commercial Pay	Overpayments			$ 104.76		$ 56.41								$ 161.17
USACE Commercial Pay	Underpayments			$ 2.03										$ 2.03
TOTAL		$ 0.57	$ 564.79	$ 108.37	$ 1.57	$ 256.29	$ 8.10	$ 5.04	$ 0.20	$ 2.89	$ 1.92	$ 0.06	$ 7.55	$ 957.35

A.   Root Causes

The following section provides additional information regarding the root causes of improper payments for each program reported in Table 6.

Military Health Benefits

External Independent Contractor (EIC) auditors manually review previously processed health care claims to identify improper payments, and to validate claims processing procedures utilized by private sector claims processors. Overpayment or underpayment errors can be assessed for (but not limited to) payments in the correct amount being sent to the wrong payee, incorrect denial of a payable claim, misapplication or calculation of a patient's deductible or co-payment/share liability, or payment of a non-covered service or supply. In FY 2016, EIC compliance reviews determined the root cause for overpayment or underpayment error assessment was the result of the following:

- Inability to Authenticate Eligibility – DHA purchased care claims processors incorrectly paid or denied a healthcare claim as a result of an incorrect patient eligibility determination.

- Administrative or Process Errors – DHA's EIC determined throughout the course of compliance reviews that DHA purchased care claims processors incorrectly processed healthcare claims by incorrectly applying a reimbursement determination or methodology when processing a healthcare claim; incorrectly calculating the Federal Government's liability after consideration of other health insurance (OHI) payment(s); based on patient healthcare claims history, incorrectly made duplicative payments for some or all of previously paid healthcare services/supplies; miscalculated the portion of the patient's healthcare responsibility either as a cost-share or benefit deductible; made a payment for services or supplies which were not a TRICARE benefit or incorrectly denied payment for services or supplies that were a TRICARE benefit; incorrectly calculated the government's reimbursement of healthcare based on a billed amount other than what was being reported on a healthcare claim form or itemized medical bill; or incorrectly based its reimbursement determination/methodology on an incorrect procedure code.

- Medical Necessity Not Evident– the claims processor failed to follow TRICARE medical necessity review policy requirements prior to processing and paying a healthcare claim, or failed to provide the medical necessity review documentation needed to support or substantiate the adjudication of the claim being reviewed during audit.

- Insufficient Documentation to Determine Payment – the claims processing documentation provided during audits by claims processors was insufficient and did not support the adjudication of the healthcare claim; as a result the EIC determined the services or procedures rendered should not have been paid.

- Other: In addition to the OMB established root cause error categories listed above, DHA established a number of individual payment error categories that can be assessed against private sector contractors during a post-payment EIC compliance review. For FY 2016 the following individual payment errors were assessed against private sector contractors:

1) Authorization/Pre-Authorization Needed – the claims processor failed to follow TRICARE authorization or pre-authorization requirements prior to processing a payment for a healthcare claim, or on audit failed to provide the authorization/prior-authorization documentation needed to support the adjudication of the healthcare claim.

2) Claims Development Required – the claims processor processed and paid a healthcare claim without obtaining additional or correct information needed to support or justify the payment of the healthcare claim, as required by TRICARE policy.

3) OHI Payment Omitted – claims documentation submitted for processing contained information of OHI payment, however the claims processor failed to consider such information when determining Government liability.

4) Diagnosis Related Group (DRG) Reimbursement Error – the claims processor made an error in calculating the reimbursement due to an institution based on the DRG reimbursement system.

5) Timely Filing Error – the claims processor processed and paid claims for benefit dates of service that did not meet TRICARE timely filing requirements, and failed to obtain the appropriate timely filing waiver(s) needed to authorize such payments.

6) Other – EIC assesses this error category when a payment error is detected but none of the other error code reasons available are applicable to the claim being reviewed. In this case the EIC auditor specifies, in its detailed audit comments, the reason for the payment error assessment.

Military Pay

The primary reason for Military Pay errors is the combination of units and service members untimely submittal of military pay documents for processing. Nearly 100 percent of the improper payments identified during this reporting period were recovered, or are in the process of being recovered.

Military Pay improper payments typically result from incorrect entitlement allocation. These entitlements are:

- Basic allowance for housing;

- Base pay for Active Duty and incorrect Active Duty pay for Reservists;

- Overseas housing allowance;

- Family separation allowance, Active and Reserve;

- Hostile fire/imminent danger pay; and

- Miscellaneous categories, which include over 25 different entitlements.

Civilian Pay

The Civilian Pay improper payments primarily were overpayments due to administrative errors caused by untimely or inaccurate entry of information into pay systems. This is in part due to the high turnover rate of civilian payroll clerks. Improper payments identified include:

- Incomplete and/or inaccurate time and attendance records,

- Late personnel actions, and

- Unsupported overseas and other allowances.

The Defense civilian payroll systems, like most government payroll systems, require time and attendance submissions occur prior to the end of the actual pay period to meet processing deadlines. Therefore, the Department must correct overpayments and underpayments in a subsequent pay period. Errors in overseas Civilian Pay accounts often occur due to payment of an entitlement that erroneously continued after the employee has returned to the United States. These improper payments often result from inaccurate personnel actions generated by human resources offices. In general, human resource offices process corrections in subsequent pay periods. These corrections result in pay and allowance re-computations and create a collection action to offset the overpayment.

Military Retirement

Over 95 percent of actual errors identified in the Death Master Files resulted from payments made by DFAS to deceased retirees or annuitants prior to DFAS receiving notification of their passing. Untimely notification of a retiree's or annuitant's death, by family members or other entities, often results in an initial, unavoidable overpayment to a deceased retiree. A review of overpayments to deceased retirees in FY 2017 disclosed that the Department recovered approximately 95 percent of overpayments within 60 days of initial notification of the retiree's or annuitant's death.

Other common errors identified through post-payment reviews included:

- Non-compliance with documented procedures,

- No documented procedure in place for retroactive Veterans Affairs award policy changes, and

- Manual computation errors.

DoD Travel Pay

The DoD Travel Pay improper payments primarily resulted from voucher input errors by travelers and/or inadequate reviews of travel vouchers by approving officials (AOs). Travel Pay errors identified in the samples can be separated into two distinct categories: administrative errors and monetary errors.

Administrative errors include missing or invalid receipts (as defined in the Joint Travel Regulations) and/or omission of required elements (i.e., dates and/or signatures).

- Receipts: Failure to attach receipts to the travel voucher, invalid or incorrect receipts, and illegible receipts.

- Signatures/Dates: Failure of travelers and/or AOs to sign and/or date the DD Form 1351-2, Travel Voucher, prior to submission by the Non-DTS Entry Agent into the Defense Travel System (DTS).

Monetary errors are payments that may have resulted in an actual loss to the government.

- Meals & Flat Rate Per Diem: Failure to properly calculate flat rate per diem (i.e., partial per diem) once a member is on travel for 31 or more days, as well a failure to pay the proper meal rate.

- Lodging: The attached receipt for lodging does not reflect the same amount claimed on the travel voucher.

- Dual lodging paid incorrectly.

- All other monetary errors, not categorized above, include a combination of 28 additional categories.

DFAS Commercial Pay

The DFAS Commercial Pay improper payments resulted from administrative errors. Administrative errors included:

- Contract input errors,

- Late payment interest penalty errors, and

- Payment processing and invoice errors.

Commercial Bill Pay Office Naples

The Commercial Bill Pay Office Naples improper payment resulted from a duplicate payment made during a reorganization of the program.

USACE Travel Pay

The USACE Travel Pay improper payments resulted from voucher input errors by travelers and inadequate reviews of travel vouchers by AOs.

USACE Commercial Pay

The USACE Commercial Pay improper payments resulted from administrative errors on contracts and insufficient documentation to support contract payments.

B.   Corrective Actions

The following section describes the corrective actions the Department has implemented or is currently in the process of implementing to reduce and prevent improper payments (IP) in the five programs determined, in FY 2017, to be susceptible to significant improper payments. According to OMB Circular No. A-123, Appendix C, "significant improper payments" are defined as gross annual improper payments (i.e., the total amount of overpayments and underpayments) in the program exceeding (1) both 1.5 percent of program outlays and $10,000,00 of all program or activity payments made during the fiscal year reported or (2) $100,000,000 (regardless of the improper payment percentage of total program outlays).

Military Heath Benefits (FY 2017 IP Amount = $150.17M)

DHA private sector contractors are monetarily incentivized or dis-incentivized, through payment accuracy performance standards, to reduce and/or eliminate improper payments. The fewer improper payments the contractors make, the less money is deducted from their reimbursements. Additionally, details of the EIC compliance reviews are shared with the private sector contractors, DHA Program Offices, private sector contract Contracting Officers (COs), and government Contracting Officer Representatives (CORs) to coordinate appropriate corrective action plans with the respective private sector contractor. Moreover:

- Upon completion of an EIC compliance review, respective contractors review results, formulate an action plan to mitigate future findings, and derive a process to avoid future improper payments;

- If warranted, contractor claims processing systems are modified to meet the Department's healthcare policy, reimbursement, or benefit requirements; and

- If audit results show a potential error pattern for a certain type of claim, additional claims are reviewed to conduct a focused study, and adjustment actions are taken as appropriate.

Each private sector contractor has its own business process for evaluating compliance review results, conducting root cause analyses to ensure the accuracy of future claims payment, and developing internal corrective action plans. If required, DHA COs and CORs issue contractor corrective action plans to resolve and track noncompliance with TRICARE healthcare policy/regulations and purchased-care contracts.

Military Pay (FY 2017 IP Amount = $182.51M)

The Department will continue providing comprehensive training and standard desk procedures to new payroll clerks to improve accuracy in processing payroll accounts. In addition, the Department, primarily through DFAS, will continue advising the Military Services of the results of payment reviews and the associated reasons for the errors. Moreover, DFAS will continue to provide the Military Services with monthly reports on the results of statistical reviews, including the reasons for and dollar value of errors and year-to-date trends, to enhance Service training.

Additionally, DFAS will continue to distribute Personnel Payment Reports to the Military Services as a way of providing the most common debts for in-service and out-of-service members. Moreover, DFAS and the Military Services will meet on a monthly basis to discuss the reasons for the debts and work to resolve them. The Military Pay Service & Business Integration Offices will also continue to validate pay and entitlement information by reconciling data between the Defense Joint Military Pay System and the Marine Corps Total Force System to Veterans Administration data and data in the Defense Enrollment Eligibility Reporting System (DEERS). These reconciliations are designed to prevent improper payments by detecting incorrect housing rates, member-to-member marriages, departed or separated service members, and "ghost" accounts.

Military Retirement (FY 2017 IP Amount = $127.58M)

The Department's control processes to prevent, identify, and reduce overpayments to deceased retirees and annuitants include:

- Validating the existence of retirees and/or annuitants living outside the United States;

- Certifying annually the existence and entitlement for all annuitants:

   o Who are under 55 years of age,

   o Who receive hard copy checks in a foreign country, and/or

   o Who have a permanent disability (regardless of age);

- Conducting periodic, random certifications for retirees over a certain age; and

- Validating military retiree's existence if payments are returned and/or if a benefit account was suspended for several months due to a bad check or incorrect correspondence address.

Early detection and data mining efforts, along with partnerships with other federal and state entities, are also used to detect improper payments. The Department takes a proactive approach to ensuring the accuracy of Military retiree payments by routinely comparing retired and annuitant payroll master file databases with the Social Security Administration's Death Master File, and periodically comparing records with the Office of Personnel Management's deceased files, Department of Veterans Affairs' database, and with individual states with sizable retiree and annuitant populations (e.g., Texas, California, and Florida). Payments for military retirees identified as deceased are suspended pending validation of death.

DoD Travel Pay (FY 2017 IP Amount = $263.34M)

Over the past five FYs, the DoD Travel Pay program has consistently reported the highest improper payment error rate among all DoD-reported programs. As a result, reducing travel improper payments and enhancing recovery efforts are major priorities of the Office of the Under Secretary of Defense (Comptroller) (OUSD(C)). OUSD(C) implemented a revised Travel Pay Remediation Plan in FY 2017, and as part of the plan, the Deputy Chief Financial Officer (DCFO) was designated as the Senior Accountable Official (SAO) for travel improper payments for the Department and the Accounting and Finance Policy (A&FP) Directorate was designated as the

Executive Agent of the DoD improper payments program. Moreover, the DCFO and A&FP Directorate implemented the revised plan by:

- Identifying SAOs at the Senior Executive Service level for travel improper payments in each of the Military Services and seven defense agencies (i.e., U.S. Special Operations Command (USSOCOM), the Defense Contract Audit Agency, the Defense Contract Management Agency, DFAS, the Defense Logistics Agency, the Defense Information Systems Agency, and the Missile Defense Agency);

- Holding quarterly progress meetings;

- Using the new DFAS Postpay Audit Compliance Tool to distribute detailed travel error reports to Components for action; and

- Developing Component corrective action plans, which included additional training for travelers and AOs, enhancements to DTS, and pre-payment reviews of vouchers by independent third-parties.

Through SAO leadership, the Military Services and six defense agencies developed and implemented travel remediation plans to improve the DoD Travel Pay program and reduce its improper payments rate. The Department's travel remediation efforts resulted in a positive reduction in travel improper payments (see Table 4) and improved metrics. With respect to metrics, DFAS overhauled its DTS post-payment review reports to provide significantly more actionable data to the applicable Military Services and defense agencies. The monthly DFAS reports were presented at the SAO meetings to highlight progress, disclose the most common types of errors, recommend corrective actions, and share best practices. The SAO structure and meetings will continue and be expanded to provide further oversight and accountability in FY 2018.

In FY 2017, DFAS launched a new post-pay database that consolidated the results of their DoD Travel Pay reviews. The database enabled DFAS to provide DoD leadership with timely, detailed information on the root causes of travel improper payments, recovery of overpayments, and other data at the Military Service and activity level by key factors such as: agency, installation, traveler and reviewer/AO, and detailed error descriptions. Specifically, the database provided information to the Department, which was used on the front-end of travel operations to reduce improper payments.

DFAS also produced multiple training videos, articles, and other online resources to inform travelers, reviewers, and AOs of the most common errors and mitigating controls to prevent them when submitting and/or approving a voucher for payment. These resources have been posted to various homepages, websites, and social media pages with the intent of impacting a wide audience

In addition, the Defense Travel Management Office enhanced DTS in July 2017 by incorporating a front-end control notification that visually alerts travelers and reviewers/AOs if required receipts are missing for certain expenses. This system enhancement should have a significant impact on travel errors related to insufficient documentation in FY 2018.

<u>USACE Commercial Pay (FY 2017 IP Amount = $163.20M)</u>

USACE is putting additional controls in place to improve the management and documentation of payments at the Contract Line Item level, where warranted. Additionally, USACE is taking corrective actions systemically within the Corps of Engineers Financial Management System (CEFMS) to automate the supporting documentation delivery process to ensure timely delivery of documentation for audit/review.

III.   Recapture of Improper Payments Reporting

Table 7 reports each program or activity that expends $1 million or more annually and either conducts a payment recapture audit or recaptures payments outside of a payment recapture audit. It also reports the amount recovered through recapture audits and amounts recovered through sources other than payment recapture audits.

A Soldier demonstrates hand-to-hand combat on a "volunteer" from the crowd during the 6th Ranger Training Battalion's open house event April 29 at Eglin Air Force Base, Fla. The event was a chance for the public to learn how Rangers train and operate. The event displays showed equipment, weapons, a reptile zoo, face painting and weapon firing among others. The demonstrations showed off hand-to-hand combat, a parachute jump, snake show, and Rangers in action.

Photo by Samuel King Jr.

Table 7: Overpayment Payment Recaptures with and without Recapture Audit Programs							
($ in millions)							
		Overpayments Recaptured through Payment Recapture Audits				Overpayments Recaptured outside of Payment Recapture Audits	
Does this include funds recaptured from a High-Priority Program (Y/N)	Program or Activity	Amount Identified in FY 2017	Amount Recovered in FY 2017	Recapture Rate in FY 2017	FY2018 Recapture Rate Target	Amount Identified in FY 2017	Amount Recovered in FY 2017
N	Military Health Benefits[1,2,3,4]					$ 128.00	$ 285.59
N	Military Pay[5]					$ 212.40	$ 173.60
N	Civilian Pay[5]					$ 57.20	$ 57.20
N	Military Retirement[6]					$ 8.52	$ 8.09
N	DoD Travel Pay[7,8]	$ 4.14	$ 2.08	50%	55%	$ 0.10	$ 0.00
N	DFAS Commercial Pay					$ 64.36	$ 59.95
N	Commercial Bill Pay Office Naples					$ 0.01	$ 0.01
N	USACE Travel Pay[9]					$ 0.94	$ 1.08
N	USACE Commercial Pay[10]					$ 2.98	$ 2.80
	TOTAL	$ 4.14	$ 2.08	50%	55%	$ 474.51	$ 588.32

[1] The amount identified in FY 2017 represents the total extrapolated overpayment dollars in the universe (FY 2017 over-payments from Table 4).

[2] The amount recovered in FY 2017 represents negative TRICARE Encounter Data (TED) transactions to DHA (recoupments) for claims in audit universes. DHA only included recoupments that occurred after each audit's end date, as recoupments occurring before an audit concluded should not be considered a recoupment due to that audit. In contrast, recoupments that occurred after an audit concluded can reasonably be expected to be a result of findings from that audit. DHA chose to report recoupments this way to match the extrapolation methodology for overpayments. Overpayments from sample results are extrapolated to represent the entire universe (reported as FY 2017 over-payments in Table 4). Therefore, DHA considers any negative payment across the universe to be a recoupment, regardless of whether the claim was randomly selected to be part of the sample. The amount recovered in FY 2017 includes recoupments for overpayments identified in audits as well as refunds occurring in the course of routine claim adjustments (for claims initially paid in FY 2016 and other fiscal years). DHA has no way to distinguish overpayment recoupments from routine claim adjustments.

[3] Recoupments for Oct15 – Sept16 TRICARE Pharmacy low dollar claims were not included in the amount recovered in FY 2017 figure because this audit was not conducted.

[4] The Active Duty Dental Program (ADDP) refunds were calculated differently. The amount recovered in FY 2017 figure for ADDP represents refunds shown on contractor invoices to DHA. ADDP data is not included in the TED system, thus contractor invoices were used because TED transactions are not available.

[5] Military Pay and Civilian Pay include in-service collections for recovery amounts. Military Pay also includes out-of-service debts. Both in-service collections and out-of-service debts continue to be collected beyond the Agency Financial Report period.

[6] The amounts identified and recovered for the Military Retirement program are based on a 100 percent review of deceased retired and deceased annuitant accounts.

[7] The DoD Travel Policy Compliance Program is the formal recapture audit program of the DoD Travel Pay program. It was mandated in the FY 2012 National Defense Authorization Act to review travel vouchers in a near real-time basis. The program scope is limited to temporary duty vouchers processed in the DTS and currently includes 13 queries that identify the most common improper payments. It is reported as part of the DoD Travel Pay program on Table 7 and reported separately on Tables 8 and 9.

[8] DFAS was not able to determine the total amounts identified and recovered for the Defense Travel System (DTS) payments due to a DTS failure and unrecoverable loss of data preventing them from completing post-payment reviews for Apr17 – Jul17, and from completing recovery and reconciliation verification for the FY. The amounts reported as recaptured outside of payment recapture audits were reported by the Army and the Air Force.

[9] The amount recovered in FY 2017 for USACE Travel Pay is greater than the amount identified in FY 2017 because the collected amount was recaptured in the current reporting year, however, the actual payment itself may have been processed in a prior reporting year. The collected amount also may include administrative fees and late payment interest.

[10] The amount recovered in FY 2017 for USACE Commercial Pay was recaptured in the current reporting year only, and does not include administrative fees and late payment interest.

Table 8 reports the disposition of funds recaptured through payment recapture audit programs.

Table 8: Disposition of Funds Recaptured Through Payment Recapture Audit Programs								
($ in millions)								
Program or Activity	Amount Recaptured[1]	Agency Expenses to Administer the Program	Payment Recapture Auditor Fees	Financial Management Improvement Activities	Original Purpose	Office of Inspector General	Returned to Treasury	Other
DoD Travel Policy Compliance Program[2, 3, 4]	$2.08	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$2.08
TOTAL	$ 2.08	$ -	$ -	$ -	$ -	$ -	$ -	$2.08

Table 9 reports an aging schedule of the amount of overpayments identified through payment recapture audit programs that are outstanding (i.e., overpayments that have been identified, but not recaptured).

Table 9: Aging of Outstanding Overpayments Identified in the Payment Recapture Audit Programs				
($ in millions)				
Program or Activity	Amount Outstanding (0 – 6 months)	Amount Outstanding (6 months to 1 year)	Amount Outstanding (over 1 year)	Amount determined to not be collectable
DoD Travel Policy Compliance Program[5, 6]	$ 0.89	$ 0.14	$ 0.63	$ 0.01
Total	$ 0.89	$ 0.14	$ 0.63	$ 0.01

[1] This amount will be identical to the "Overpayments Recaptured through Payment Recapture Audits - Amount Recovered in FY 2017" in Table 7.
[2] IPERA mandates that only funding that is expired at the time of collection can be reallocated for the purposes identified in Table 9. As such, only $0.65M of the $2.08M recaptured was eligible for reallocation.
[3] A re-allocation process has been developed and an initial test was conducted with the Air Force to prove the process. During the test $3,184.00 was reallocated as follows: $1,447.00 to the Defense Travel Management Office for Agency Expenses to Administer the Program; $1,447.00 for Original Purpose; $290.00 to the Office of Inspector General (US Air Force). Evaluation is ongoing to determine if the cost of automation will be beneficial to DoD.
[4] $0.65M was eligible for reallocation under IPERA. Other than the amount reallocated during the test, the funds remained as collected in the original appropriations. The DoD Financial Management Regulation directs funds that are not reallocated to remain in the original account until cancelled.
[5] Amounts outstanding are identified errors, in which, no corrective actions have been taken to resolve them. Errors that have been corrected or errors that are currently in the collection process are not included.
[6] Amount determined not to be collected are errors identified during FY 2017 that are uncollectible due to one of the following reasons: debt of $10 or less, waiver approved, or out-of-service debt.

DoD Travel Policy Compliance Program

In December 2012, the Department established the DoD Travel Policy Compliance Program, mandated by the *National Defense Authorization Act for FY 2012*. Managed by the Defense Travel Management Office, the program was established to ensure travel claims do not exceed reasonable or actual expenses as well as to minimize inaccurate, unauthorized, overstated, inflated, or duplicate travel claims. The DoD Travel Policy Compliance Tool, an automated application (separate and distinct from the DFAS Postpay Audit Compliance Tool), reviews paid DTS travel vouchers in near real time and identifies potential improper payments. If a potential improper payment is identified, travelers and their AOs are notified via e-mail to either submit a corrected claim or explain why the claim is correct. Service administrators can run reports to review all identified errors and track corrections.

The DoD Travel Policy Compliance Tool assists in recouping funds by tracking which identified improper payments have been corrected and repaid, and reporting on which identified errors have not been corrected. It also improves post-payment audits, educates travelers and administrators on travel policy, and identifies opportunities for greater controls in the future. As of September 30, 2014, all DoD Components using DTS are actively using the Compliance Tool, and all DTS vouchers are being examined using 13 areas of inquiry. During FY 2017:

- $4.14 million in errors were identified, and

- $2.08 million was recovered resulting in a recapture rate of 50 percent.

In addition to examining DTS vouchers, the Compliance Tool has expanded to include additional data sources, such as Government Travel Charge Card (GTCC) data, and is now comparing amounts claimed on vouchers with amounts charged on the GTCC to identify potential overpayments. Also, it now incorporates debt data from DTS to record recoveries against identified improper payments. Use of the Compliance Tool provides a mechanism to greatly facilitate the Department's collections and improve the recovery rate for Travel Pay overpayments. In addition, funds recovered from prior years may be re-allocated for use in current year appropriations, in accordance with IPERA.

Defense Health Agency

DHA utilizes a number of different mechanisms to prevent, identify, and collect improper payments. These include claims auditing by an EIC, contractor utilization of DHA's Duplicate Claims System, and periodic independent reviews of private-sector payments. This process utilizes post-payment review techniques, performed internally and by external contractors. Overpayment recoveries are returned to the Military Health Benefits program.

Contract payments comprise a large volume of transactions with high-dollar values; therefore, DHA is vigilant to ensure payment accuracy. In addition to the post-payment reviews, DHA also utilizes various internal manual and automated prepayment initiatives to prevent overpayments and underpayments. During FY 2016, DHA recovered $285.59 million in overpayments as a result overpayment errors identified by the EIC, refunds occurring in the course of routine claims adjustments, and ongoing private sector contractor internal audits.

Defense Finance and Accounting Service

The Department continues to use its internal staff and procedures to identify and recover overpayments. The DFAS recovery percentages remain above the 85th percentile, as required by OMB.

In compliance with IPERIA, as well as the *Debt Collection Improvement Act of 1996*, the Department uses a number of other methods to prevent, identify, and collect improper payments. For example, DFAS implemented a Centralized Offset Program to look across the Components for opportunities to offset debts within the first 90 days of delinquency. Once this deadline passes, DFAS transfers the debts to the Department of the Treasury, no longer waiting until day 120 as allowed by statute, to utilize all debt collection tools available earlier in the debt lifecycle to increase the likelihood of collecting the debt. During FY 2017, the Centralized Offset Program requested and confirmed 756 offsets totaling approximately $11.6 million.

U.S. Army Corps of Engineers

USACE uses a data mining tool as part of its post payment/payment recapture program. This tool searches for potential errors, such as duplicate, missing, or irregular invoices, as well as specific types of recurring payments. If the data mining tool identifies errors, USACE takes appropriate action to correct them and recover any overpayments. There are ten scenarios built into the data mining tool, which searches 100 percent of all USACE commercial payments. The use of a data-mining tool complements the prepayment system edits built into the Corps of Engineers Financial Management System. Payment safeguards include a requirement to match a receiving report with an invoice and thereby prevent use of duplicate invoice numbers for the same obligation.

U.S. Air Force F-35 Lightning II's from Hill Air Force Base, Utah, fly in formation during a training flight May 2, 2017. The F-35s are participating in their first-ever flying training deployment to Europe.

Photo by Senior Airman Christine Groening

Other Information

IV.   Barriers

The Department did not identify any statutory or regulatory barriers limiting its corrective actions in reducing improper payments in those programs determined in FY 2017 to be susceptible to significant improper payments.

V.   Accountability

The Under Secretary of Defense (Comptroller)/Chief Financial Officer is the Accountable Official for the Department and is responsible for ensuring that, to the greatest extent possible, all DoD disbursements are accurate.

The Department adheres to title 10, United States Code, *section 2773(a)*, which holds Departmental Accountable Officials (DAOs), including AOs, accountable for government funds. DAOs/AOs are subject to pecuniary liability for an illegal, improper, or incorrect payment. This law forms the basis of the DoD Financial Management Regulation (*DoD FMR*), *Volume 5, Chapter 5*, "Certifying Officers, Departmental Accountable Officials, and Review Officials." Moreover, the Department's efforts to recover overpayments are administered in accordance with the debt collection policy promulgated in DoD FMR, *Volume 16*, "Department of Defense Debt Management".

The DoD FMR contains other policies that specifically address improper payments (DoD FMR *Volume 4, Chapter 14*) and recovery auditing (DoD FMR *Volume 10, Chapter 22*). The Office of the Deputy Chief Financial Officer, A&FP Directorate is the Executive Agent of the DoD improper payments program and its associated reporting requirements. This Directorate provides oversight to the program by providing guidance and ensuring all Components adhere to applicable IPERA laws and regulations.

Over the past five FYs, the DoD Travel Pay program has consistently reported the highest improper payment error rate among all DoD-reported programs. As a result, reducing travel improper payments and enhancing recovery efforts were major priorities of OUSD(C). OUSD(C) implemented a revised Travel Pay Remediation Plan in FY 2017, and as part of the plan, the DCFO was designated as the Senior Accountable Official (SAO) for travel improper payments for DoD. Moreover, a key part of the implementation plan was the identification of SAOs for travel improper payments in each of the Military Services and seven defense agencies. Based on the positive results recognized in the DoD Travel Pay program, SAO responsibilities will be expanded, in FY 2018, to include the other improper payments program areas.

In addition, a new tool was introduced to the DoD improper payment program in FY 2017 to track corrective action progress. The Notification of Findings and Recommendations (NFR) Tracker will be used to monitor audit recommendations and corrective actions. This tool provides a method to record corrective actions for each improper payment program, to set milestones and interim goals, and to monitor progress toward more long-term objectives. The tool will also be configured to notify officials when milestone dates are approaching, and also will require a justification when a milestone or deadline is missed.

VI.   Agency Information Systems and Other Infrastructure[17]

The Department has the information and infrastructure needed to reduce improper payments. For instance, DoD uses the Business Activity Management (BAM) tool and the Do Not Pay (DNP) portal as front-end controls to prevent improper payments prior to disbursement.

The majority of commercial payments are input into the BAM tool, which is a pre-payment control that evaluates payment data against a series of business rules called "integrity checks," and, if payment exceptions are generated, requires users to review exception data against source systems and supporting documentation. Since the implementation of the BAM tool in August 2008, it has prevented a significant amount of improper payments in the Department's commercial payment systems. Continued analysis of payment errors has enhanced BAM logic and improved disbursement accuracy. In FY 2017, DFAS enhanced the BAM tool through the successful implementation of an interface with the Defense Enterprise Accounting and Management System (DEAMS). This interface provides insight into potential improper payments within the DEAMS entitlement system in a pre-payment environment.

The DNP portal is a multi-functional analytics tool that allows the Department to check various data sources for pre-award, pre-payment eligibility verification, at the time of payment and any time in the payment lifecycle. It also allows disbursing Components to verify eligibility of a vendor, grantee, loan recipient, or beneficiary prior to payment and helps to prevent, reduce, and stop improper payments, as well as prevent fraud, waste, and abuse.

Moreover, the Department's ongoing migration from legacy systems to new Enterprise Resource Planning systems presents a number opportunities to prevent and detect improper payments. This migration may also enhance the Department's ability to improve its debt collection and recovery auditing abilities.

Military Health Benefits

DHA has much of the information and infrastructure needed to reduce improper payments. DHA Purchased Care Program (managed by the Contract Resource Management (CRM)) includes an immense volume of claims processed by private sector contractors. To track these programs, CRM utilizes the following systems:

- TRICARE Encounter Data (TED). TED is a financial feeder system, through which all claims are processed to Oracle Federal Financials. TED is the entry point of claims information from DHA private sector contractors. TED records provide detailed information for each treatment encounter and are submitted as either an institutional or non-institutional record. TED is primarily required by DHA to account for the expenditure of government funds, develop statistical information, and is as a data source of record for EIC audits. Records submitted through the TED System (TEDS) must pass numerous validation edits prior to being accepted into TEDS.

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[17] In accordance with OMB *Circular No. A-136*, this section is applicable to only those programs with improper payments exceeding the statutory thresholds listed in OMB Circular No. A-123, *Appendix C*, Part I.A.9. Step 1, and therefore determined in FY 2017 to be susceptible to significant improper payments.

- E-Commerce System (ECS). ECS is an integrated, centralized major system that improves DHA's core financial, contracting and business process by providing seamless integrated financial and contracting systems.

- Oracle Federal Financials (OFF). OFF is the financial subsystem of the DHA ECS. It supports budget and accounting/financial functions and healthcare (TEDS) claims processing and contains TRICARE Claims Management, Accounts Receivable, Accounts Payable, Purchase Orders and the General Ledger modules. CRM uses OFF to track commitments and obligations. These transactions are submitted to DFAS and become the primary source into financial statements.

In addition to internal DHA financial systems, DHA private sector contractor's claims processing systems are developed and designed in accordance TRICARE System Manual requirements and contain numerous systems edits. These edits include patient eligibility (verified via the Defense Enrollment Eligibility Reporting System (DEERS)), provider eligibility, and more. If a claim passes initial eligibility edits, benefit calculations occur based on programmed payment rules and reimbursement methods determined by TRICARE Reimbursement Policy. The claims processing systems are able to determine the appropriate reimbursement methodology based on information included in the healthcare claim such as type of service, claim form type, provider specialty, etc.

Further, DHA has developed the TRICARE Duplicate Claims System (DCS). This tool facilitates the identification of duplicate claim payments, the initiation and tracking of recoupments required by purchased care contractors, and the ultimate cancellation of duplicate records from the TEDS database. DHA purchased care contractors are contractually required to use the DCS and resolve duplicate payments.

Military Pay

A new system, the Integrated Personnel and Payment System (IPPS), has been slated to replace the Defense Joint Military Pay System (DJMS). It is an integrated pay and personnel system being designed to mitigate risks by reducing duplicate key-stroking thereby increasing the accuracy and timeliness of payment inputs from Command groups, human resource activities, pay activities, and Service Members. This system is currently scheduled to be phased in by 2020.

DoD Travel Pay

In FY 2017, DFAS launched a new post-pay database that consolidated the results of their DoD Travel Pay reviews. The database enabled DFAS to provide DoD leadership with timely, detailed information on the root causes of travel improper payments, recovery of funds, and other data at the service and activity level. This additional detail provided the services with data by key factors such as: agency, installation, traveler and reviewer/approving official, and detailed error descriptions. Specifically, the database provided information to the Department, which was used on the front-end of travel operations to reduce improper payments.

Moreover, the Defense Travel Management Office (DTMO) enhanced DTS with a receipts notification function that alerts travelers and AOs if required receipts for certain expenses are

missing prior to submitting travel vouchers for payment. This enhancement directly impacts one of the top five errors (i.e., insufficient or lack of documentation) identified in the DoD Travel Pay program. In addition, DTMO is also planning to add a Flat Rate per Diem control into DTS in FY 2018 to mitigate the leading error identified in the DoD Travel Pay program. This enhancement or front-end control will eliminate manual computations for travelers by automating the calculation of flat rate per diem for long-term travel. Also, the Department continues to use and enhance the DTMO DoD Travel Policy Compliance Tool as discussed in the Payment Recapture Audit Reporting section of this report.

Paratroopers assigned to 1st Battalion, 501st Parachute Infantry Regiment, 4th Infantry Brigade Combat Team (Airborne), 25th Infantry Division, U.S. Army Alaska, jump out of a Nevada Air National Guard C-130H Hercules while conducting airborne training at Joint Base Elmendorf-Richardson, Alaska, April 13, 2017. The Soldiers of 4/25 belong to the only American airborne brigade in the Pacific and are trained to execute airborne maneuvers in extreme cold weather/high altitude environments in support of combat, partnership and disaster relief operations.

Photo by Alejandro Pena

VII.   Sampling and Estimation[18]

The primary disbursing Components use statistically valid sampling methods designed to meet or exceed OMB's requirements of a 90 percent confidence level and a margin of error of ±2.5 percent. By using these methods, disbursing Components are able to identify valid sample sizes and project improper payment percentages for the Department's improper payment programs. The smaller disbursing Components normally perform 100 percent post payment reviews or a full review of payments above a specific dollar threshold, with random sampling for lower dollar payments.

Military Health Benefits

DHA defines samples (sets strata boundaries, calculates sample sizes, and randomly selects claims for review) and the EIC reviews the selected claims to identify improper payments. Payment accuracy compliance reviews include two sample types: a payment sample (to ensure payment accuracy by identifying underpayment and overpayments) and a denied payment sample (to ensure appropriate claim denial). Paid samples are conducted as a stratified random sample based on paid amounts and denied samples are conducted as a stratified random sample based on billed amounts. Samples are drawn on either a quarterly or semi-annual basis, respective of DHA purchased care contract requirements.

- Payment Sample: Paid samples are conducted to identify improper payments and measure payment accuracy. Depending on the private sector contract type, the universe for a paid sample may contain between several hundred thousand to 30 million claims. All claims with government payment amount above a high-dollar threshold (i.e., $200,000) are reviewed by the EIC. Claims between the high-dollar threshold and a low-dollar threshold (i.e., $100) are randomly sampled based on stratification of the government payment amount and reviewed by the EIC. Claims below the low-dollar threshold are not included in EIC audits (but are represented by DHA Low-Dollar Internal Reviews).

  - Samples for paid claims include between four and 12 strata, depending on the composition of the claims in the universe. Mathematical formulas are utilized to identify optimal strata boundary points, and sample sizes are calculated to meet (or exceed) an estimate with a minimum of 90 percent confidence plus or minus 2.5 percentage points (as stipulated in the OMB Circular No. A-123, Appendix C, guidelines).

- DHA Low-Dollar Internal Review: In addition to the EIC reviews, DHA conducts a statistically valid internal review of low-dollar claims that fall below the low-dollar threshold for payment samples and are thus excluded from EIC audits. Audits for these internal reviews are stratified if appropriate, given the composition of the universe data.

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[18] In accordance with OMB *Circular No. A-136*, this section is applicable to only those programs with improper payments exceeding the statutory thresholds listed in OMB Circular No. A-123, *Appendix C*, Part I.A.9. Step 1, and therefore determined in FY 2017 to be susceptible to significant improper payments.

- Denied Payment Sample: The primary purpose of the denied payment samples is to ensure that health care/supplies are not being denied inappropriately (which may represent obstacles in TRICARE beneficiaries' access to care) by private sector contractors. Records that encompass the denied payment sample universe are limited to records with government payment amount equal to zero. All denied claims with a billed amount above a high-dollar threshold are reviewed, and claims below this threshold are randomly sampled based on stratification of the billed amount. Depending on the contract type, a denied audit universe may contain between several thousand to over one million claims.

    o The denied payment sample is similar in design to the payment sample; the primary difference is that the denied sample is stratified based on billed amount since the paid amount for a denied claim is equal to $0.

- Combining the Samples: Results from the payment sample, denied sample, and DHA's internal low-dollar review are combined to calculate the overall improper payment rate for the Military Health Benefits program.

Military Pay

DFAS designed the program samples using a dollar-stratified sampling plan and the Neyman Allocation method. The Neyman Allocation method stratifies financial data from the Defense Joint Military Pay System (DJMS) and the Marine Corps Total Force System (MCTFS) and allocates the data to defined strata. The overall variable sample size was calculated for the combined systems to produce a point estimate with a 95 percent confidence interval and a margin of error of ±2.5 percent. Samples were then randomly selected using the Statistical Package for the Social Sciences (SPSS) statistical software from each system's population as a whole. Each payment within each stratum had an equal probability of selection.

On a monthly basis, DFAS statistically sampled Military Pay accounts stratified by Active Duty (i.e., Army, Navy, Air Force, and Marine Corps) and Reserve Components (i.e., Army Reserve, Army National Guard, Navy Reserve, Air Force Reserve, Air National Guard, and Marine Corps Reserve), and further stratified by the dollar amount of disbursements. The Defense Management Data Center provided the total universe of military pay accounts for each branch and component. DFAS reviewed the sampled pay accounts and calculated estimates of improper payments.

Military Retirement

On a monthly basis, DFAS statistically sampled military retirement payments stratified by retired and annuitant pay accounts. The reviews contained samples of: drilling reserve units, retiree offsets, survivor benefit plans, transfers to/from the Temporary Disability Retired List to the Permanent List, and Veterans Affairs offsets. The overall variable sample size was calculated to produce a point estimate with a 95 percent confidence interval and a margin of error of ±2.5 percent.

In FY 2018, DFAS will update its Military Retirement sampling plan to a methodology that stratifies the population by the status of the account (e.g. new accounts, accounts with changes, and unchanged accounts).

DoD Travel Pay

DFAS designed the program samples using a dollar-stratified sampling plan and the Neyman Allocation method. The Neyman Allocation method stratifies financial data from the Defense Travel System (DTS) and the Windows Integrated Automated Travel System (WinIATS) and allocates the data to defined strata. The overall variable sample size was calculated for the combined systems to produce a point estimate with a 95 percent confidence interval and a margin of error of ±2.5 percent. Samples were then randomly selected using SPSS statistical software from each system's population as a whole. Each payment within each stratum had an equal probability of selection.

On a monthly basis, DFAS sampled vouchers from the Defense Travel System (DTS) stratified by component (i.e., Army, Navy, USMC, Air Force, and defense agencies) and vouchers from the WinIATS stratified by travel type (i.e., Active, Reserve, Casualty, Contingency, Civilian Permanent Change of Station (PCS), Defense Agencies, International Military Education and Training, Military PCS, Navy Reserve Officers' Training Corps, and Navy Travel). In addition, each population was further stratified by dollar amount.

DFAS statisticians selected a random sample and the Postpay Review and Analysis team reviewed the samples and calculated estimates of improper payments. Furthermore, to form the overall DoD Travel Pay improper payments estimate, the DFAS DTS and WinIATS improper payment estimates were combined with the Army's WinIATS estimates of overseas travel, the Navy's WinIATS estimate, the Air Force's Reserve Travel System estimate, and the U.S. Marine Corps' WinIATS estimate.

In FY 2018, DFAS will segregate USSOCOM from the DTS Defense Agencies population and sample it separately in order to provide USSOCOM with more detailed information regarding the root causes of their travel errors. DFAS selected USSOCOM because it accounts for the largest number of travel vouchers amongst the Defense Agencies.

USACE Commercial Pay

The USACE post payment compliance reviews were conducted using a statistically valid, 95 percent confidence level and a margin of error of ±2.5 percent, sample taken from the entire USACE Commercial Pay universe. USACE implemented a revised sampling plan in July 2017. This plan is a variable design, stratified by dollar amount performed for the period of July - June. Samples are drawn on a quarterly basis for review. The purpose of the sampling plan is to estimate the percentage of commercial payments in error as well as provide sample statistics on the dollar value of over and under payments (improper payments) for use in annual IPERIA reporting. In addition, the USACE Finance Center used prepayment controls, post payment contract audits, and data mining to identify and prevent improper payments in Commercial Pay.

VIII. Significant Accomplishments

The Department is committed to full compliance with the requirements of IPERIA and the Federal Improper Payments Coordination Act of 2015. As part of the Department's audit efforts, each disbursing Component is diligently reviewing and reporting all payments subject to IPERIA and the Federal Improper Payments Coordination Act of 2015, as well as examining processes for identifying the complete universe of payments.

Moreover, the Department continues to explore measures to improve its front-end internal controls to prevent improper payments, and strengthen post payment review teams to recover identified improper payments. Also, the Department is actively implementing recommendations from the following audit reports:

- DoD Inspector General 2016 report, "The DoD Did Not Comply With the Improper Payment Elimination and Recovery Act in FY 2016" (Report No. *DODIG-2017-078*); and

- Government Accountability Office 2013 report, "Significant Improvements Needed in Efforts to Address Improper Payment Requirements" (Report No. *GAO-13-227*).

Accordingly, OUSD(C) implemented a revised Travel Pay Remediation Plan by identifying SAOs for travel improper payments in each of the Military Services and seven Defense Agencies, holding quarterly progress meetings, using the new DFAS Postpay Audit Compliance Tool to distribute detailed travel error reports for action, and developing Component corrective action plans. OUSD(C)'s travel remediation efforts resulted in a 2.24 percent reduction in travel improper payments and improved metrics. As a result, SAO responsibilities will be expanded in FY 2018 to include the other improper payments program areas.

Also, the Department continued to adopt best practices related to statistical sampling and improved system controls, procedures, and guidance. In FY 2017, DFAS revised the sampling plans for the Civilian Pay, Military Pay, and Travel Pay programs from simple random sample designs to stratified random sample designs; DFAS also assisted the Department of the Navy with generating commercial and travel pay sampling results by using its Commercial Pay and Travel Pay revised stratified sampling plans; and USACE revised its sampling plans for its Commercial Pay and Travel Pay programs from simple random sample designs to stratified random sample designs. In FY 2018, DFAS will segregate the Mechanization of Contract Administration Services (MOCAS) system from the commercial systems population and sample it separately in order to improve the representation of the non-MOCAS commercial systems. MOCAS routinely accounts for approximately 60 percent of the Commercial Pay sample population every quarter. In addition, OUSD(C) obtained the services of a statistician to provide objective oversight and further assess Component sampling methodologies for each program, to ensure each yield statistically valid improper payment estimates.

Moreover, OUSD(C) began an initiative to identify the universe of entitlement and disbursing systems for each improper payment program. This initiative directly supports the assertion of completeness by validating that all payments are subject to review for improper payments. While the validation of the universe of payments will require extensive coordination and considerable time, OUSD(C) expects to make significant progress in FY 2018 as the

Department begins full financial statements audit. Preventing and recovering improper payments are among the top financial management priorities of DoD.

For additional information on improper payments not included in the FY 2017 AFR, refer to *PaymentAccuracy.gov*.

A U.S. Marine Corps AH-1Z Cobra assigned to Marine Aviation Weapons and Tactics Squadron One (MAWTS-1) lands during the final exercise (FINEX) two as part of Weapons and Tactics Instructor course (WTI) 2-17 at Yuma Ariz., April 27, 2017. The FINEX exercise is designed to execute a simulated special operating forces raid while simultaneously supporting regimental combat team objectives and focusing on conducting all six functions of Marine Aviation. WTI is a seven-week training event hosted by MAWTS-1 cadre, which emphasizes operational integration of the six functions of Marine Corps aviation in support of a Marine Air Ground Task Force and provides standardized advanced tactical training and certification of unit instructor qualifications to support Marine Aviation Training and Readiness and assists in developing and employing aviation weapons and tactics.

Photo by Cpl. AaronJames B. Vinculado

FRAUD REDUCTION REPORT

The Fraud Reduction and Data Analytics Act of 2015 (*FRDAA*) was enacted on June 30, 2016 to help improve the ability of Federal agencies to prevent, detect, and respond to fraud. Under the FRDAA, the Office of Management and Budget (OMB) was required to establish guidelines for Federal agencies to (1) establish financial and administrative control activities in order to identify and assess fraud risks and (2) design and implement control activities in order to prevent, detect, and respond to fraud, including improper payments. The FRDAA specifies that these OMB guidelines must incorporate the leading practices identified in the July 2015 Government Accountability Office (GAO) *Report No. GAO-15-593SP*, "A Framework for Managing Fraud Risks in Federal Programs." In addition to the establishment of guidelines, the FRDAA required the OMB to establish a working group to improve the sharing and development of fraud-related data analytics and controls leading practices.

To establish accountability, the FRDAA requires each Federal agency to report on their progress in:

- Implementing (1) financial and administrative controls in compliance with the OMB guidelines, (2) the fraud risk principle in the GAO Standards for Internal Control in the Federal Government ("*Green Book*"), and (3) OMB *Circular No. A-123* leading practices for managing fraud risk;

- Identifying risks and vulnerabilities to fraud; and

- Establishing strategies, procedures, and other steps to curb fraud.

In FY 2017, the Department began its efforts to comply with the requirements of the FRDAA. As a first step in this effort, the Department is conducting a coordinated fraud risk assessment throughout the DoD Components (including the Military Departments) to ascertain the extent of control activities currently in place related to the prevention, detection, and response to fraud. The results of this assessment will inform the Department of any gaps and shortfalls from the FRDAA requirements and enable the development of a comprehensive DoD-wide Fraud Risk Management Framework and strategy for the prevention, detection, and response to fraud. Once developed, the Fraud Risk Management Framework will guide the Department's efforts in implementing integrated fraud risk assessment and related fraud control processes across the Department.

Also in response to the requirements of the FRDAA, the Department participated in multiple meetings with the OMB working group tasked with overseeing the scope and development of an interagency library of data analytics tools and data sets and informing the government-wide strategy to manage fraud risk. During FY 2017, the OMB working group developed a plan to leverage existing data analytic programs and resources developed by third-party organizations (such as the Committee of Sponsoring Organizations of the Treadway Commission, the Association of Certified Fraud Examiners, and the Association of Government Accountants) and accomplished the compilation of an initial inventory of tools and materials, which is currently available for use by Federal agencies.

REDUCE THE FOOTPRINT

The Department of Defense (DoD) supports the principles set out by the Office of the Management and Budget (OMB) in Section 3 of OMB *Memorandum-12-12*, OMB Management Procedures *Memorandum No. 2013-02*, and the *National Strategy* for the Efficient Use of Real Property (2015-2020), by continually striving to identify opportunities for reduction in the total square footage of the domestic DoD office and warehouse inventory. As a result of the Department's infrastructure consisting mainly of assets that are not typically candidates for consolidation or reuse by other Federal agencies, a significant portion of the reduction in DoD footprint continues to be in the form of demolition. However, because demolition incurs an initial cost to produce future savings in operating cost, budget cuts and continuing resolutions have had a negative impact on the Department's ability to secure the necessary funding for the demolition of assets identified for disposal.

As such, Tables 10 and 11 reflect an increase in both the Department's square footage and operating expenses related to office and warehouse space reported for FY 2016 over the FY 2015 baseline. This increase resulted from shifts in the Department's strategic deployment (such as the expansion of DoD operations into new or expanded locations) which necessitated the construction or acquisition of additional square footage, while assets identified for demolition continued to persist due to budgetary constraints. To remediate this situation, the Department continues to advocate for authority to pursue opportunities for Base Realignment and Closure action as a more realistic means of reduction.

Table 10. Reduce the Footprint Policy Baseline Comparison			
	FY 2015 Baseline	FY 2016	Change (FY 2016 – FY 2015 Baseline)
Square Footage (in millions)	339.3	355.0	15.7

Table 11. Reporting of O&M Costs – Owned and Direct Lease Buildings			
	FY 2015 Reported Cost	FY 2016	Change (FY 2016 – FY 2015 Baseline)
Operation and Maintenance (O&M) Costs ($ in millions)	$ 829.5	$ 903.6	$ 74.1

CIVIL MONETARY PENALTY ADJUSTMENT FOR INFLATION

On November 2, 2015, the President signed into law the Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 (*the 2015 Act*), which further amended the Federal Civil Penalties Inflation Adjustment Act of 1990 (*the Inflation Adjustment Act*). The 2015 Act, requires Federal agencies to annually adjust applicable civil monetary penalties for inflation to improve the effectiveness and retain the deterrent effect of such penalties. The implementation of this rule will deter violations of law, encourage corrective action(s) of existing violations, and prevent waste, fraud, and abuse within the Department of Defense.

Table 12. FY 2017 Civil Monetary Penalty Adjustments for Inflation						
Name of Penalty*	Authority (Statute)	Year Enacted	Year of Previous Adjustment	Year of Current Adjustment	Current Penalty Level ($ Amount)	Sub-Agency/Bureau/Unit
Unauthorized Activities Directed at or Possession of Sunken Military Craft	National Defense Authorization Act for FY 2005, 10 U.S.C 113, note	2004	2016	2017	$126,626.00	Department of the Navy
Unlawful Provision of Health Care	10 U.S.C. 1094(c)(1)	1985	2016	2017	$11,119.00	Defense Health Agency
Wrongful Disclosure — Medical Records: First Offense Subsequent Offense	10 U.S.C. 1102(k)	1986	2016	2017	$6,5759.00 $43,832.00	Defense Health Agency
Violation of the Pentagon Reservation Operation and Parking of Motor Vehicles Rules and Regulations	10 U.S.C. 2674(c)(2)	1990	2016	2017	$1,811.00	Deputy Chief Information Officer
Violation Involving False Claim	31 U.S.C. 3802(a)(1)	1986	2016	2017	$10,957.00	Office of Inspector General
Violation Involving False Statement	31 U.S.C. 3802(a)(2)	1986	2016	2017	$10,957.00	Office of Inspector General

* Penalty updates can be found at *81 Federal Register 62629 – 62631*.

GRANTS OVERSIGHT & NEW EFFICIENCY ACT REQUIREMENTS

The Grants Oversight & New Efficiency *(GONE) Act* was enacted on January 28, 2016 with the goal of helping Federal agencies to more efficiently identify and close out expired grants. To accomplish this, the Act requires the head of each agency to submit a report to Congress which identifies and quantifies federal grant awards (including cooperative agreements) which have been expired for more than 2 years but have not been closed out. Table 13 below provides a subset of the information to be reported to Congress by December 31, 2017 in response to the requirements of the GONE Act.

Table 13. Expired DoD Federal Grant and Cooperative Agreement Awards as of November 5, 2017			
CATEGORY	2-3 Years	>3-5 Years	>5 Years
Number of Grants/Cooperative Agreements with Zero Dollar Balances	1,717	1,198	846
Number of Grants/Cooperative Agreements with Undisbursed Balances	858	224	174
Total Amount of Undisbursed Balances	$138,804,185.69	$110,226,692.23	$14,812,146.67

The Department has been affected by multiple factors which have led to delays in its efforts to properly closeout federal grant awards in a timely manner:

- Lack of adequate staffing,

- Missing reports from grantees (including patent reports),

- Discrepancies between final cost reports and payment reports,

- Late calculation/receipt of final rates, and

- Delays caused by litigation settlements.

The Department is actively researching and seeking to implement strategies to mitigate these challenges in the grant closeout process. For instance, in response to the negative impact of inadequate staffing the Department increased the number of personnel whose job duties are dedicated to closing federal grant awards in FY 2017, including the hiring of additional experienced senior staff to review documentation and oversee the closeout process. Combined with other process improvements which have been implemented during FY 2017, the Department is already realizing benefits in its federal grant award closeout process, with expired awards being closed more rapidly than in the past.

SUMMARY OF THE DOD OFFICE OF THE INSPECTOR GENERAL'S TOP MANAGEMENT CHALLENGES

Each year, the Department of Defense (DoD) Inspector General (IG) prepares a statement summarizing the most serious management and performance challenges facing the Department and provides a brief assessment of the Department's progress in addressing these challenges. The IG management challenges were identified based on a variety of factors, including DoD OIG oversight work, research, and judgment; oversight work done by other DoD components; oversight projects conducted by the Government Accountability Office; and input from DoD officials.

For FY 2018[19], the DoD IG identified challenges in the following ten categories:

- Countering Strategic Challenges: North Korea, Russia, China, Iran, and Transnational Terrorism

- Addressing Challenges in Overseas Contingency Operations in Iraq, Syria, and Afghanistan

- Enabling Effective Acquisition and Contract Management

- Increasing Cyber Security and Cyber Capabilities

- Improving Financial Management

- Maintaining the Nuclear Enterprise

- Optimally Balancing Readiness, Modernization, and Force Structure

- Ensuring Ethical Conduct

- Providing Effective, Comprehensive, and Cost Effective Health Care

- Identifying and Implementing Efficiencies in the DoD

The DoD IG's memorandum and report on "Top Management and Performance Challenges Facing the Department of Defense – FY 2018" may be found in Appendix E, reprinted in its entirety as published.

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[19] This year's IG summary of challenges is for FY 2018 rather than for FY 2017. In previous years, the document's title contained the year of the DoD financial statement that included the report. While last year's report was labelled as FY 2016, this year the IG labelled the document as the top management challenges for FY 2018 to reflect its forward-looking orientation. Therefore, no document is labelled FY 2017 summary of management challenges, but there has been no gap in IG top management challenges documents.

U. S. Air Force and U.S. Marine Corps explosive ordnance disposal technicians prepare a hole for a range detonation in Southwest Asia, Feb. 11, 2017. These essential technicians respond to in flight emergencies and properly dispose of hazardous or unserviceable explosives and ammunition.

Photo by Staff Sgt. Eboni Reams

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