



FY 2018

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Summary of Financial Statement Audit and Management Assurances

Department of Defense (DoD or the Department) 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 the DoD mission. As discussed in 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 over 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;
- FMFIA Section 2, Effectiveness of Internal Control over Operations; or
- FMFIA Section 4, Compliance with Federal Financial Management Systems Requirements / FFMIA Section 803(a), Implementation of Federal Financial Management Improvements.



Marines march in formation during the Sunset Parade at the Lincoln Memorial in Washington, D.C., July 17, 2018. The Marines are assigned to Marine Barracks Washington.

Marine Corps photo by Staff Sgt. John A. Martinez Jr.

Summary of Financial Statement Audit

Exhibit 1 lists the 20 areas of material weaknesses in the Department's financial statement reporting as identified by the DoD Inspector General ([DoD IG](#)) in the Independent Auditor's Report. The material weakness areas identified by DoD IG in the Independent Auditor's Report are consistent with those identified by DoD management (which are identified using the assessable unit categories as defined by the DoD Enterprise Risk Management and Internal Control Program) with three exceptions: Environmental and Disposal Liabilities, Entity Level Controls, and Oversight and Monitoring. The Department concurs with DoD IG's conclusions and will focus on implementing the necessary corrective actions to address each of the material weaknesses noted by the DoD IG in the Independent Auditor's Report.

Environmental Liabilities

The Department assessed Environmental and Disposal Liabilities (E&DL) in FY 2018 and concluded material weaknesses reported by the Department of the Army and the Department of the Air Force were resolved due to the implementation of an E&DL methodology framework used to produce auditable E&DL estimates and standardize the business practices of reporting active E&DLs. However, the DoD IG identified additional deficiencies within the DoD E&DL approach. The Department concurs with DoD IG's conclusions and will initiate further efforts to substantiate the completeness and valuation of Environmental Liabilities.

Entity Level Controls

During FY 2018, the Department enhanced and updated enterprise-wide guidance documents and tools to assist DoD Components with the establishment and testing of entity-level internal controls; however, implementation of these resources was not completed in FY 2018. The Department concurs with DoD IG's conclusions and will continue to prioritize the implementation of entity-level controls at the DoD Component level to mitigate the risk of material misstatements on the DoD Components' and the Agencywide principal financial statements.

Oversight and Monitoring

Although some DoD Components did not report corrective action plans (CAPs) in FY 2018 for all of their material weaknesses, the Department develops enterprise-wide CAPs through the use of subject matter experts to support the coordination of remediation efforts to address auditor-issued notices of findings and recommendations (NFRs). The Department concurs with the DoD IG's conclusions and will continue to use the NFR Database to track the status of CAPs and validate that they are designed to implement timely and effective corrective actions to remediate all DoD material weaknesses. The status of DoD CAPs will continue to be regularly reported to the Financial Improvement and Audit Remediation Governance Board and the Defense Business Council.

Exhibit 1. Summary of Financial Statement Audit*Audit Opinion: Disclaimer**Restatement: No*

Material Weakness	Beginning Balance	New	Resolved	Consolidated	Ending Balance
Accounting Entries ¹	1			(1)	0
Financial Management Systems and Information Technology ^{2,3}	1				1
Universe of Transactions ⁴	0	1			1
Financial Statement Compilation	0	1			1
Fund Balance with Treasury	1				1
Accounts Receivable ⁵	1				1
Operating Materials & Supplies	1				1
Inventory and Related Property	1				1
General Property, Plant, and Equipment ⁶	1				1
Government Property in Possession of Contractors ⁷	1				1
Accounts Payable ⁸	1				1
Environmental and Disposal Liabilities	1				1
Legal Contingencies ⁹	0	1			1
Beginning Balances ⁹	0	1			1
Journal Vouchers ¹⁰	0	1			1
Intragovernmental Eliminations ⁸	1				1
Statement of Net Cost ⁹	1				1
Reconciliation of Net Cost of Operations to Budget ⁹	1				1
Budgetary Resources ¹⁰	0	1			1
Entity Level Controls	0	1			1
Oversight and Monitoring	0	1			1
Total Material Weaknesses	13	8	0	(1)	20

Exhibit 1 Footnotes:

¹ The Accounting Entries material weakness identified by the DoD IG in the DoD Agency Financial Report for FY 2017 was consolidated into the Journal Vouchers material weakness identified by the DoD IG in FY 2018.

² The Financial Management Systems and Information Technology material weakness identified by the DoD IG was titled Financial Management Systems by the DoD IG in the DoD Agency Financial Report for FY 2017.

³ The Financial Management Systems and Information Technology material weakness identified by the DoD IG is included within the Federal Financial Management Systems Requirements material weakness identified by DoD management in Exhibit 6.

⁴ The Universe of Transactions material weakness identified by the DoD IG is included within the Federal Financial Management Systems Requirements material weakness identified by DoD management in Exhibit 6.

⁵ The Accounts Receivable material weakness identified by the DoD IG is included within the Reimbursable Work Orders material weakness identified by DoD management in Exhibit 2.

⁶ The General Property, Plant, and Equipment material weakness identified by the DoD IG includes the Equipment Assets and Real Property Assets material weaknesses identified by DoD management in Exhibit 2.

⁷ The Government Property in Possession of Contractors material weakness identified by the DoD IG is included within the Accountability and Management of Property Furnished to Contractors for the Performance of a Contract material weakness identified by DoD management in Exhibit 2.

⁸ The Accounts Payable and Intragovernmental Eliminations material weaknesses identified by the DoD IG are included within the Health Care Liabilities, Military Pay, Contract/Vendor Pay, Reimbursable Work Orders, and Transportation of Things material weaknesses identified by DoD management in Exhibit 2.

⁹ The Legal Contingencies, Beginning Balances, Statement of Net Cost, and Reconciliation of Net Cost of Operations to Budget material weaknesses identified by the DoD IG are included within the Financial Reporting Compilation material weakness identified by DoD management in Exhibit 2.

¹⁰ The Journal Vouchers and Budgetary Resources material weaknesses identified by the DoD IG are included within the Fund Balance with Treasury material weakness identified by DoD management in Exhibit 2.

Summary of Management Assurances

FMFIA Section 2, Effectiveness of Internal Controls over Financial Reporting

Under the oversight of the DoD Financial Improvement Audit Remediation Governance Board, the Department's assessment of the effectiveness of its internal controls over financial reporting resulted in the downgrade of three previously reported material weaknesses in FY 2018. Exhibit 2 lists the FY 2018 material weaknesses in internal controls over financial reporting, captured by end-to-end process and assessable unit, and reports the changes from the material weaknesses disclosed in the DoD Agency Financial Report ([AFR for FY 2017](#)).

Exhibit 2. FY 2018 Effectiveness of Internal Control over Financial Reporting (FMFIA §2)

Statement of Assurance: No Assurance

End-to-End Process	Assessable Unit	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Budget-to-Report	Fund Balance with Treasury (FBWT)	3					3
	Financial Reporting Compilation	6					6
Hire-to-Retire	Health Care Liabilities	2					2
	Military Pay	3					3
Procure-to-Pay	Contract/Vendor Pay	6					6
	Reimbursable Work Orders	3					3
	Transportation of Things ¹	2				(2)	0
	Equipment Assets	2					2
Acquire-to-Retire	Real Property Assets ²	1				1	2
	Environmental Liabilities ³	1				(1)	0
	Accountability and Management of Property Furnished to Contractors for the Performance of a Contract	1					1
	Internal Use Software (IUS)	1					1
Plan-to-Stock	Inventory	4					4
	Operating Materials & Supplies (OM&S)	3					3
	Requisitioning Process (Customer Orders)	2					2
Total Material Weaknesses		40	0	0	0	(2)	38

¹ In FY 2018, Transportation of Things was reassessed and is no longer reported as a Department-wide area of material weakness.

² In FY 2018, the descriptions for Real Property Assets were divided into two areas so that material weaknesses have increased visibility of corrective actions and alignment with notifications of findings and recommendations.

³ In FY 2018, Environmental Liabilities was reassessed and is no longer reported as a Department-wide area of material weakness.

Exhibit 3. Internal Control over Financial Reporting Corrective Action Plans

Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
<u>Fund Balance with Treasury</u>	FY 2005	Department-wide		FY 2019
- 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.			- 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 accurate, documented, and resolved in a timely 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 of appropriations received and apply reconciliations back to at least FY 2013. - Obtain 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.	
<u>Financial Reporting Compilation</u>	FY 2005	Department-wide		FY 2002
- Ineffectively designed processes and controls to prepare accurate financial statements supported by general ledger balances that align with strategic performance plans to ensure compliance with Generally Accepted Accounting Principles (GAAP) and the DoD Financial Management Regulation (FMR). - Inability to reconcile detail-level transactions with the general ledgers and provide adequate supporting documentation for adjusting entries. - Accounting balances are unsupported due to inadequate financial management systems and related processes and procedures. - Inconsistency between documented processes and procedures versus actual procedures performed in practice regarding reconciliations and resolving differences.			- Revise standard operating procedures and control descriptions to incorporate the requirements of OMB-A-136, and improve variance analysis and annual financial report review procedures. Implement Standard Financial Information Structure (SFIS) to standardize financial reporting that aligns with the Department's mission. - Obtain population of feeder system transactional data and perform reconciliations from feeder systems to the general ledgers and financial statements. - Establish process to govern posting logic changes within DoD accounting systems; consolidate, categorize, document, and prioritize system requirements for changes to enable correct posting logic compliance issues. - Obtain supporting documentation at the transaction level to support adjustments; complete root cause analysis to identify true source of errors, and correct transactions at the source. Track, maintain, and analyze adjustments to verify materiality at the individual and aggregate levels to assist with addressing underlying root causes.	

• Lack of developed approach for performing reconciliations and retaining data for sensitive activities. • Inconsistent procedures for recording Journal Vouchers and Standard Business Transactions. Supporting documentation retention procedures also pose a significant risk to producing accurate and complete financial statements and reports.			• Establish guidelines for reconciliation variances that need to be resolved and require relevant service providers to post corrections in a timely manner. • Develop approach for performing reconciliations and retaining data for sensitive activities.
<u>Health Care Liabilities</u>	FY 2003	Department-wide	FY 2025
• 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.			• 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 2025.
<u>Military Pay</u>	FY 2011	Department-wide	FY 2020
• 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.			• 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.
<u>Contract/ Vendor Pay</u>	FY 2003	Department-wide	FY 2025
• 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.			• 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. • Monitor 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.

- Current systems and processes do not enable matching the contract award to accounting data for public transparency, (e.g., Data Act).
- Lack of timely contract closeout and de-obligation of funds limits the Department's access to capital.

- Develop department-wide contract closeout standard operating procedures to ensure financial systems are in balance and de-obligation 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.

<u>Reimbursable Work Orders</u>	FY 2011	Department-wide	FY 2022
	• Lack of evidence of performance, acknowledgement of receipt of intragovernmental goods and services, and validity of open obligations. • Inability to verify the timeliness and accuracy of disbursements and validate recorded reimbursable agreements. • Ineffective process to collect, exchange and reconcile buyer and seller intragovernmental transaction.		• 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 of periodic reviews, and identify and implement standard enterprise reconciliations that provide for validation of the seller/buyer-side balances and input of supported journal vouchers for timing differences.

<u>Equipment Assets</u>	FY 2006	Department-wide	FY 2022
	• 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, accuracy and transfer from Construction in Progress (CIP) to the general equipment account.		• Implement Federal Accounting Standards Advisory Board Technical Bulletin 2017-2 and the associated DoD General Equipment (GE) Financial reporting responsibilities policy memo to align financial reporting of GE assets with the accountability of the assets. • Publish and leverage results of the go-forward equipment valuation study which provides a consistent and streamlined methodology for balance sheet reporting of GE assets across the department. • DoD Components are continuing to develop and implement aspects of their "go forward" approach for valuing Equipment and sustaining these values (including CIP) in accordance with GAAP; as well as modifying their Accountable Property

System of Records (APSR) to ensure they capture the required data.

- Continue to leverage the Defense Audit Remediation Working Group for expedited policy guidance and update the DoD Financial Management Regulation chapters for accounting for military and general equipment, as required.
- DoD Components to continue to validate asset listings for completeness and accuracy and document process and control environments.
- DoD Components to continue to apply controls and procedures to manage property accountability, including adequate documentation to support acquisition and disposal processes throughout the year.
- Continue to convene the GE Working Group and DoD Component Property Lead property accountability workshops to highlight policy and guidance gaps impacting the valuation of GE, report on quarterly progress in establishing accountable records, and use as a forum for sharing lessons learned.

Real Property Assets	FY 2000	Department-wide	FY 2019
<i>Existence and Completeness</i>			
• Real property processes, controls and supporting documentation do not substantiate that (1) all existing assets are recorded in an APSR, (2) all assets recorded in the APSR properly reflect DoD's legal interest in the asset.		• Implement and regularly conduct a lifecycle process for a real property physical inventory: ◦ 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. ◦ Ensure adequate documentation is available to support existence and completeness and placed in service dates. • Complete floor-to-book and book-to-floor baseline reconciliation of real property assets with adequate documentation to support existence and completeness.	
<i>Valuation, Rights & Obligations, Presentation, and Disclosure</i>			FY 2021
• Real property processes, controls and supporting documentation do not substantiate that, (1) all real property assets are properly valued and, (2) documentation for all real property assets properly support rights and obligations, and are appropriately presented and consistently reported in the financial statements. DoD has insufficient internal controls and supporting documentation to ensure timely recording, accuracy and the transfer of Construction in Progress (CIP) to the appropriate real property account upon completion of construction or improvements.		• Implement processes and controls to support DoD policies related to financial reporting of real property. • Document and implement go-forward processes and control environment for all lifecycle processes to include: acquisition (and CIP); inventory; reconciliation of CIP and APSR with financial statements and tenant agreements and records and disposal.	

			Establish systems to properly account for and value real property assets, including CIP. 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.
<u>Accountability & Management of Property Furnished to Contractors for the Performance of a Contract</u>	FY 2011	Department- wide	FY 2020
In FY 2011, the Department did not have clear guidance and had not properly trained Program Office staff, contract specialists, and accountable property officers regarding policies and procedures for appropriately managing property provided to a contractor (this includes both contractor acquired property (CAP) and Government Furnished Property (GFP). As a result, DoD's accountability records are incomplete. Audit reports have consistently identified a lack of accountability concerning GFP and CAP, for which DoD has title but not immediate physical control.			- Continue to roll out and leverage the electronic DoD enterprise solutions for standard GFP transactions via Defense Logistics Management Standards within the Wide Area Work Flow /Procurement Integrated Enterprise Environment applications. - Continue to review metrics such as GFP contract clause compliance, assertion packages, and APSRs for each component and provide analysis of progress towards accountability. - Components are evaluating current execution and improving guidance and business processes to ensure accountability of GFP and CAP. Components are also continuing to review existing contracts and establish accountability over legacy GFP. - Continue to hold GFP Working Group meetings to share lessons learned, discuss Notice of Findings and Recommendations (NFRs) and corrective action plans (CAPs), resolve identified problems, and promote usage of new electronic GFP transaction solutions.
<u>Internal Use Software</u>	FY 2015	Department- wide	FY 2022
The Department has not properly addressed the management and financial reporting of Internal Use Software (IUS), which is required by Statement of Federal Financial Accounting Standards (SFFAS 10) and must be addressed through updated guidance in the Financial Management Regulation			- DoDI 5000.76, Accountability and Management of Internal Use Software, was signed March 2, 2017, and FMR Vol4, Chapter Internal Use Software was issued in August 2018 to provide accountability of an accounting for IUS. - OSD IUS Tiger Team was established to document all WHS IUS and collect lessons learned to be used Department-wide. - Components are continuing to identify and establish accountability over existing IUS and identifying new acquisitions to ensure capital IUS costs are captured and reported appropriately in accordance with Generally Accepted Accounting Principles. - Components are continuing to develop and implement processes and system changes to APSRs to properly capture and sustain proper accountability and accounting of IUS. - Evaluate DoD-wide compliance for IUS APSR requirements via data calls and

		leverage results to drive IUS APSR requirement and policy changes.	
		- Continue to convene the IUS working group to highlight policy and guidance gaps impacting the accountability and accounting of IUS, report on progress in establishing IUS accountable records and implementing sustainable processes for IUS, and use as a forum for sharing lessons learned. - Validate corrective actions in conjunction with DoD Chief Information Officer through results of standalone audits, DoD-wide audit, agency Statement of Assurance's, and information presented by Components at IUS working group.	
<u>Inventory</u>	FY 2005	Department-wide	FY 2022
	- 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.		- Develop methodology and inventory condition code reports to support a monthly JV related to inventory, including retention of supporting documentation for all inventory transactions and related JVs. - Conduct periodic inventories and reconciliation of inventory accounts to validate systems of record are performed. Draft revisions to DoDM 4140.01 Volume 5. Implement methodology to value inventory in the absence of historical costs (for baseline of asset inventory). - Improve assurance that inventory recorded in the financial statements exist and is complete through publication of ADC 1244 "Establishing Visibility of Unique Item Tracking Program Items for Service-Owned Assets Stored at DLA Distribution Centers and Corresponding Revisions to Inventory Procedures Related to Capital Equipment" In June 2018. - 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.
<u>Operating Materials & Supplies (OM&S)</u>	FY 2005	Department-wide	FY 2022
	- Historical cost data is not maintained; 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		- Draft revisions to DoDM 4140.01 V5 to support the initiatives to require 100% Annual Inventory (to establish a baseline and/or as a corrective measure); and address issues with co-mingling. - Integrated Process Team (IP) migrating weaknesses associated with the lack of Material Receipt Acknowledgements and developing methodology and inventory condition code reports supporting monthly inventory related JVs; , including retention of key supporting documentation (KSDs) for all inventory transactions and related JVs. - Identify and document the current inventory reconciliation processes,

inventories are not accounted for in DoD accountable property systems.

including key controls and financial transactions.

- Establish GAAP-compliant valuation methodologies that include appropriate acquisition cost approaches to support all audit assertions of OM&S.

Requisitioning Process (Customer Orders)

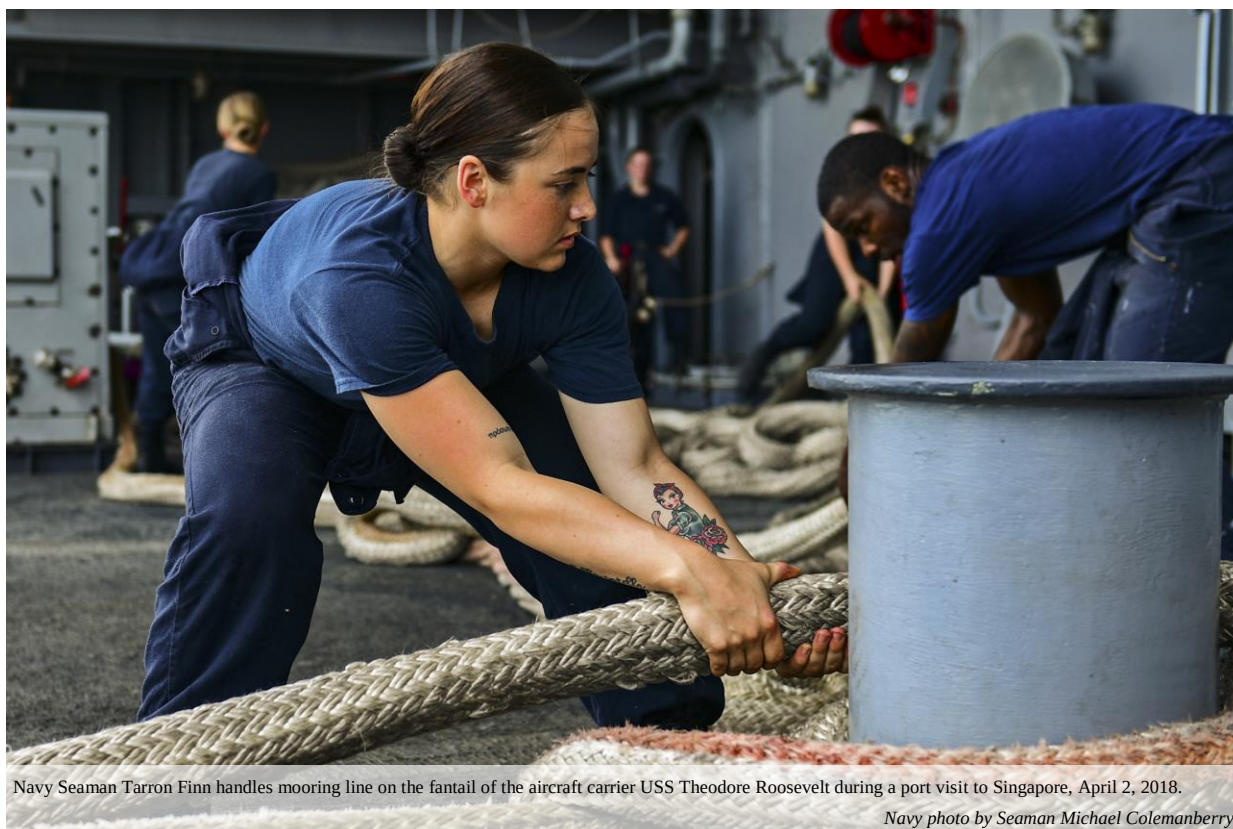
FY 2013

Department-wide

FY 2020

- Off-line requisition systems lack interfaces with the supply and financial automated systems to ensure timely recording of obligations.
- The Component's supply and financial systems do not interface with DLA and GSA offline requisition systems.

- Implement system interfaces based on approved Defense Logistics Management Standards for requisitioning and internal ordering.
- Conduct testing to validate system interfaces.



Navy Seaman Tarron Finn handles mooring line on the fantail of the aircraft carrier USS Theodore Roosevelt during a port visit to Singapore, April 2, 2018.

Navy photo by Seaman Michael Colemanberry

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. Exhibit 4 lists the FY 2018 material weaknesses in the internal controls over operations, captured by operational area, and reports the changes from the material weaknesses disclosed in the DoD AFR for FY 2017.

Exhibit 4. FY 2018 Effectiveness of Internal Controls over Operations (FMFIA §2)

Statement of Assurance: Modified Assurance

Assessable Unit	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Acquisition ⁴	2				(1)	1
Comptroller and/or Resource Management	1					1
Communication	0	1				1
Contract Administration	3					3
Information Technology	2					2
Force Readiness	1					1
Manufacturing, Maintenance, and Repair	0	1				1
Personnel and/or Organizational Management ^{5 6}	2	4			(1)	5
Operations	0	1				1
Security	1					1
Support Services	2					2
Supply Operations	1					1
Total Material Weaknesses	15	7	0	0	(2)	20

⁴ In FY 2018, Acquisition reassessed a material weakness (MW) for DoD acquisition program oversight, which was determined not to be a systemic issue and was downgraded.

⁵ In FY 2018, Personnel and/or Organizational Management split an existing MW into five MWs and added information to include hiring process deficiencies.

⁶ In FY 2018, Personnel and/or Organizational Management reassessed and downgraded a MW for Adjudicating personnel matters of up to >18 Months.

Exhibit 5. Effectiveness of Internal Controls over Operations Corrective Action Plans

Areas of Material Weakness	Year Identified	DoD Components	Corrective Actions	Target Correction Year
<u>Acquisition</u> Lack of Program Executive Office Program Manager acquisition lifecycle oversight mandated by the DoD 5000 series of policies and regulations. Additionally, the organizational structure is non-compliant with the 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 2017	Defense Health Agency, Defense Threat Reduction Agency	- 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
<u>Comptroller and/or Resource Management</u> Ineffective internal controls and management oversight for processes such as management of improper payments and use of 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.	FY 2019
<u>Communication</u> The Department of the Air Force (AF) has identified a systemic issue in communication of security information between installations and appropriate external entities (e.g., the Federal Bureau of Investigation).	FY 2018	Department of the Air Force	- Identify digital fingerprinting hardware and software. - Identify partnering solution with AF Office of Special Investigations. - Security Forces Management Information System Replacement. - Long-term software solution for case management.	FY 2023
<u>Contract Administration</u> - The Department must strategically manage Services Acquisition, define outcomes, and capture data to facilitate strategic management of the acquisition function. - The Department continues to face challenges meeting fiscal year competition goals and needs to address	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. - Publication of a revised DoDI 5000.74, "Acquisition of Services" as required by the National Defense Authorization Act (NDAA) for FY 2017, Sec. 803, projected for FY 2019.	Reassessed annually

ill- suited contract arrangements and utilize incentives. • The acquisition workforce is not appropriately sized, trained, nor equipped to meet the Department's needs.		• Continue publication of DoD quarterly competition achievement; continue to implement the April 2016 DoD publication, "Guidance on Using Incentive and Other Contract Types" when selecting and negotiating a contract type.
<u>Information Technology</u> • DoD financial and business management systems and processes do not provide reliable, timely, nor accurate information. • 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 contribute to data protection vulnerabilities. Issues exist in policy compliance with cybersecurity measures, oversight, and accountability.	FY 2010 Department-wide	• Expand review and analysis of proposed information technology (IT) systems. Update the DoD Instruction (DoDI) 5000.75 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. • 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 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. FY 2020 Reassessed annually
<u>Force Readiness</u> • 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
<u>Manufacturing, Maintenance, and Repair</u> • Multiple audits and studies identified a wide range of control issues that cumulatively create material weaknesses in ship depot maintenance. Policies for defining, costing, and executing maintenance all require improvement to correctly predict both cost and duration of depot maintenance.	FY 2016 Department of the Navy	• Q1 FY 2018 – Identified obstacles to execution performance. • Q2 FY 2018 – Identified variance between Execution Year Guidance (EYG) to President's Budget and developed mitigations. FY 2020

- Q4 FY 2018 – Integrated depot maintenance in assessable units Managers’ Internal Control Program.
- Q4 FY 2018 – Established the President’s Budget as the baseline for execution year variance tracking.

<u>Personnel and Organizational Management</u>	FY 2018	Department-wide	
• Average civilian time-to-hire in the Department increased by 40% (from 70 to 106 days) between FY 2013 and FY 2017.		• In FY 2018 the Department required all components to develop and execute data-based Action Plans to reduce time to hire. The Department’s initial goal is to reduce average time to hire from 106 to 85 days or less by the end of FY 2019.	FY 2019
• The Department does not systematically collect data on hiring manager satisfaction with process or with quality of candidates for civilian positions.		• In FY 2019 the Department will start collecting hiring quality and satisfaction data; after determining baseline measures, the Department will establish future quality / satisfaction goals consistent with results achieved by other large federal agencies. Expect initial results in FY 2020.	FY 2020
• The Department manages its civilian workforce under 66 personnel systems, over 60 pay systems, and scores of special Human Resource (HR) authorities and flexibilities. This has caused excessive complexity and variability in HR processes.		• The Department is undertaking procedures to simplify, streamline, and standardize its HR processes and to provide more cost-effective HR services. The Department intends to pursue legislative relief where necessary to reduce complexity and increase efficiency of HR processes. Expect initial results in FY 2020.	FY 2020
• DoD HR specialists and managers lack training and tools to master the complex civilian federal hiring process.		• The DoD HR Functional Community was formally organized in FY 2018 to define and assess HR competencies, establish learning standards, and develop career paths. Expect initial results in FY 2021.	FY 2021
• The Department has multiple civilian personnel HR service providers operating within and across components but no systems to define, collect, monitor, or analyze their performance or cost data, nor to monitor and control the types of services provided.		• Execute HR Service Delivery project (HR Reform lead) to define, monitor, and evaluate key performance and efficiency measures for Defense Agency Field Agency (DAFA) HR Service providers; identify and remedy instances of fragmentation, overlap, and duplication; and address inefficiencies and implement reforms. Transition to single SaaS/Cloud civilian human capital management system initially for core HR transactions (mid-2019), and eventually for integrated talent management (i.e., performance management, learning, compensation, awards, workforce and succession planning). (Joint IT, HR, FM Reform project continuing through FY 2023.)	FY 2023

<u>Operations</u>	FY 2018	Department of the Navy	FY 2019
• The Department of the Navy experienced an unacceptable number of tragic surface fleet incidents in the first 8 months of 2017, and conducted two reviews (the Comprehensive Review (CR) and the Strategic Readiness Review (SRR) in early FY 2018 to determine root causes.		• Re-establish readiness as a priority. • Match supply and demand. • Establish clear command and control relationships. • Promote a learning culture that learns from experience, following root cause analysis, and trains personnel to avoid future accidents.	

- Address broader recommendations focused on the force and the overall culture of operational risk management, training and department organization.
- The Department of the Navy established a Readiness Reform and Oversight Council (co-chaired by the Under Secretary of the Navy and the Vice Chief of Naval Operations) to oversee comprehensive CR/SRR corrective action encompassing 117 specific recommendations identified in the CR/SRR playbook.

<u>Security</u>	FY 2017	Department of the Navy	Reassessed annually
• 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.		• 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.	
<u>Support Services</u>	FY 2005	Department-wide	FY 2020
• 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 (DoD IG) findings. DoD IG report indicates 37% 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. • 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. The Department continues to confront decades-old management weaknesses related to its business functions that support these forces.		• Generate requirements for internal audit / review of the performance of operations and their compliance with laws, regulations, and policies and document in the 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 DoD senior leadership routinely. • Adopt a reorganization under the new Chief Management Officer in accordance with the NDAA for FY 2018. Initiate expanded Department-wide continuous process improvement (CPI) training, develop CPI experts, and promote continuous and visible leadership support for transformation.	

Supply Operations	FY 2011	Department-wide	Reassessed annually
Government Accountability Office identified several Department-wide weaknesses in the areas of asset visibility and materiel distribution.		- Established plans of actions and milestones to address service chain management (SCM) operations through better asset visibility and distribution processes. - Published and now executing the 2017 Strategy for improving DoD Asset Visibility. The Strategy provides the framework for DoD Components to work collaboratively to provide accurate, reliable, and timely data to enhance visibility of assets throughout their lifecycle, thereby transforming asset data into actionable information in support of logistics decision making and improved customer confidence. - Published and implemented the 2016 Materiel Distribution Improvement Plan focused on performance measures, data reliability, policy, and governance. - Progress is monitored quarterly by the Logistics Executive Steering Committee.	



A U.S. sniper fires his weapon from a combat rubber raiding craft at targets placed across a lake while a Canadian sniper watches during the Europe Best Sniper Team Competition at Grafenwoehr training area, Germany, July 28, 2018.

Army photo by Kevin S. Abel

FMFIA Section 4, Compliance with Federal Financial Management Systems Requirements

In accordance with FMFIA section 4, the Department requires that all DoD financial systems comply with federal financial management systems requirements. In FY 2018, the Department reported three instances of pervasive non-conformance related to these requirements. Exhibit 6 lists the number of instances of non-conformance with federal financial management systems requirements and reports the changes from the instances of non-conformance disclosed in the DoD AFR for FY 2017.

Exhibit 6. FY 2018 Compliance with Federal Financial Management System Requirements (FMFIA §4)

Statement of Assurance: No Assurance

Non-Conformance	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
Federal Financial Management Systems Requirements	3					
Total Non-Conformances	3	0	0	0	0	3

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

Section 803(a) of the FFMIA requires each federal agency to implement and maintain financial management systems that comply substantially with (1) federal financial management systems requirements, (2) applicable federal accounting standards, and (3) the United States Government Standard General Ledger ([USSGL](#)) at the transaction level. Exhibit 7 lists the instances of non-compliance with federal financial management systems requirements.

Exhibit 7. FY 2018 Implementation of Federal Financial Management Improvements (FFMIA §803(a))

	Agency	Auditor
Federal Financial Management Systems Requirements	Lack of Compliance Noted	Lack of Compliance Noted
Applicable Federal Accounting Standards	Lack of Compliance Noted	Lack of Compliance Noted
USSGL at Transaction Level	Lack of Compliance Noted	Lack of Compliance Noted

Exhibit 8. Compliance with Federal Financial Management System Requirements Corrective Action Plans

Non-Conformance	Year Identified	DoD Components	Corrective Actions	Target Correction Year
<u>Business System Modernization</u> Ineffective processes and controls to reconcile transactions posted to the Department's Fund Balance with Treasury (FBWT) accounts with the Treasury's records.	FY 2001	Department-wide	<u>Business System Modernization and FFMIA Compliance</u> - In calendar years 2019 through 2022, the Department is scheduled to reduce the number of legacy IT audit relevant systems by 26. - To date, a total of 22 of 25 Other Defense Organizations (ODOs) have been migrated to a common ERP system, the Defense Agencies Initiative (DAI). There are three additional ODOs scheduled for deployment in FY 2019 through FY 2021. The DAI application and the data center hosting location Defense Information System Agency (DISA) both received unmodified SOC 1 reports for FY 18. DAI is an FFMIA compliant Oracle ERP COTS solution. - With the assistance of the Joint Interoperability Test Command, OUSD(C) worked with the Department financial system owners to complete SFIS compliance assessments for 28 systems through FY 2018. Assessments for an additional 26 systems are currently planned through FY 2020. The SFIS requirements are aligned to and consistent with FFMIA requirements. Currently, the Department is assessing which systems require SFIS compliance assessments. - OUSD(C) updated the Internal Control Guide in April 2018 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 (FSD) concurrent with audit readiness status.	FY 2028
<u>FFMIA Compliance</u> The Department's financial systems currently do not provide the capability to record financial transactions in compliance with FFMIA, current federal financial management requirements, applicable federal accounting standards, and the Treasury USSGL at the transaction level.	FY 2001	Department-wide		
<u>General & Application Controls</u> The DoD IT 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 originally designed to support functional purposes, such as human resource management, property management, and logistics management. These systems were not originally created 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	FY 2001	Department-wide	- OUSD(C) has established a database, FSD, to identify applications and hosting locations that impact DoD financial statement audits and track the auditor feedback regarding system controls reliance. As of June 30, 2018, DoD Reporting Entities and Service Organizations had identified a total of 246 systems relevant to financial statement audit. This number is expected to change as the system environment evolves and the financial statement audits mature. - The MILDEPS continue to deploy ERP solutions to their Commands along with software upgrades, implement System Change Requests (SCRs) and standup formal enterprise monitoring programs for transitioning to a Risk Management Framework (RMF). In addition, the Department is integrating audit relevant IT	FY 2025

and automated application controls (including security management, access, segregation of duties, configuration management, system interfaces, master data, and audit trails).

controls into the RMF system accreditation process (for systems that impact financial statement audits) and the target date for incorporating this as a requirement is FY 2019.

- In 2005, DoD service organizations began to obtain System and Organization Control (SOC 1) Reports for systems and hosting services. For FY 2018, DoD Service Organizations have obtained 14 unmodified opinions and 6 modified opinions. This includes two new SOC 1 reports and scope expansions to existing SOC 1 reports in FY 2018. Reporting entities and their auditors have been instructed to provide feedback on the SOC 1 reports and service organizations have also been instructed to provide plans for SOC1 scope expansions and additional SOC 1 reports.
- OUSD(C) has implemented a database to track auditor NFRs and associated corrective action plans. A CFO IT Functional Council was established in April 2018 to report on the status of IT NFRs and associated CAPs, identify common IT issues, share solutions, and identify instances where common solutions are needed.



Payment Integrity

The reduction of improper payments⁷ and compliance with the Improper Payments Elimination and Recovery Act of 2010 ([IPERA](#)) continue to be top financial management priorities for the Department. In FY 2018, the Department identified \$574 billion in payments subject to testing under IPERA and an improper payment rate less than 1%. Given the large dollar amount of DoD payments, this percentage represents over a billion dollars in overpayments and underpayments.

As shown in Exhibit 9, the Department identified approximately \$1 billion (0.21% of total outlays subject to testing under IPERA) as improper payments based on statistically projected testing results. Of this improper payment amount, \$665 million (0.12% of total outlays subject to testing under IPERA) was estimated to be monetary losses to the Department. Payments identified as improper do not always represent a monetary loss. For instance, an otherwise legitimate payment that lacks sufficient supporting documentation or approval is reported as improper. Moreover, based on the improper payment testing results in FY 2018, the Department's estimated proper payments were \$573 billion.

The Department complies with the requirements of federal improper payments legislation⁸ through the activities of its Payment Integrity Program. This program is comprised of eight separate programs that report improper payments for six categories of pay/benefits (civilian pay, commercial pay, military health benefits, military pay, military retirement, and travel pay). These programs collectively encompass the majority of payments made by the Department annually. Of the eight programs reporting improper payments in FY 2018, five programs (Military Health Benefits, DoD Travel Pay⁹, Commercial Pay, U.S. Army Corps of Engineers ([USACE](#)) Travel Pay, and USACE Commercial Pay) met their self-imposed improper payment target rates and three programs (Military Pay, Civilian Pay, and Military Retirement) did not. However, all eight programs reported improper payment estimates below the IPERA statutory threshold of 10%.

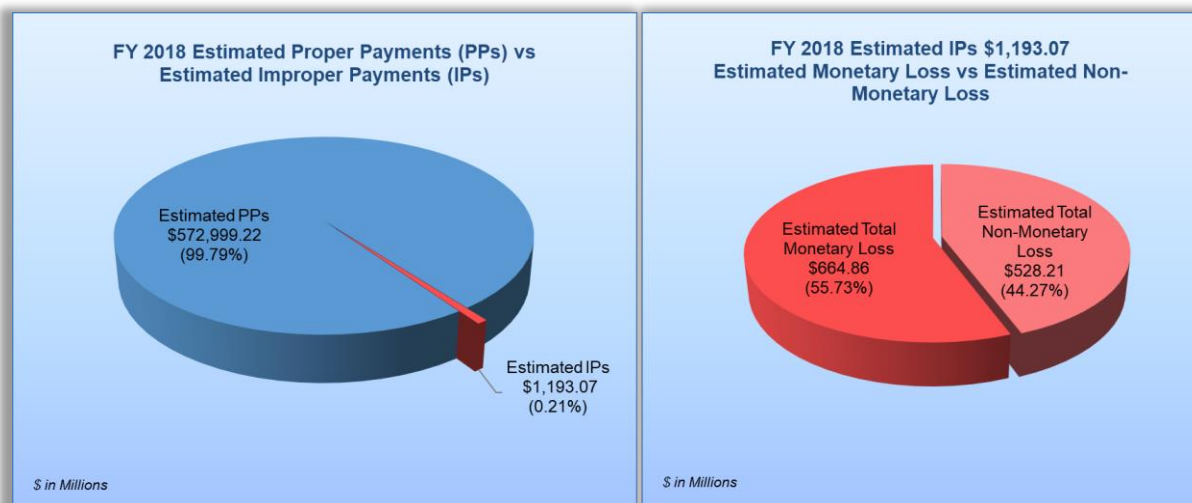
When improper payments are identified by the Department as a result of sampling and testing payments within the eight programs, DoD Components conduct evaluations to identify their root causes. Corrective action plans (CAPs) are then developed by the DoD Components to remediate the root causes. The CAPs include milestones or actions that are to be completed by specific dates. Depending on the complexity of the CAPs, execution of the plan may occur over multiple fiscal years until the root causes are fully remediated.

The Department continues to improve payment accuracy in all of its programs to ensure the billions of dollars in federal funds it disburses annually reach intended recipients in the right amount and for the right purpose. Through responsible stewardship and accountability, the Department is committed to earning the trust and confidence of Congress and the American people.

⁷ 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 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). Additionally, when an agency's review is unable to discern whether a payment was proper as the result of insufficient or lack of documentation, the payment must be considered an improper payment.

⁸ Improper Payments Information Act of 2002 ([IPIA](#)), as amended by the Improper Payments Elimination and Recovery Act of 2010 ([IPERA](#)) and the Improper Payment Elimination and Recovery Improvement Act of 2012 ([IPERIA](#))

⁹ In FY 2018, the DoD Travel Pay program met its self-imposed improper payment target rate for the first time in six consecutive fiscal years.

Exhibit 9. FY 2018 Estimated Proper and Improper Payments

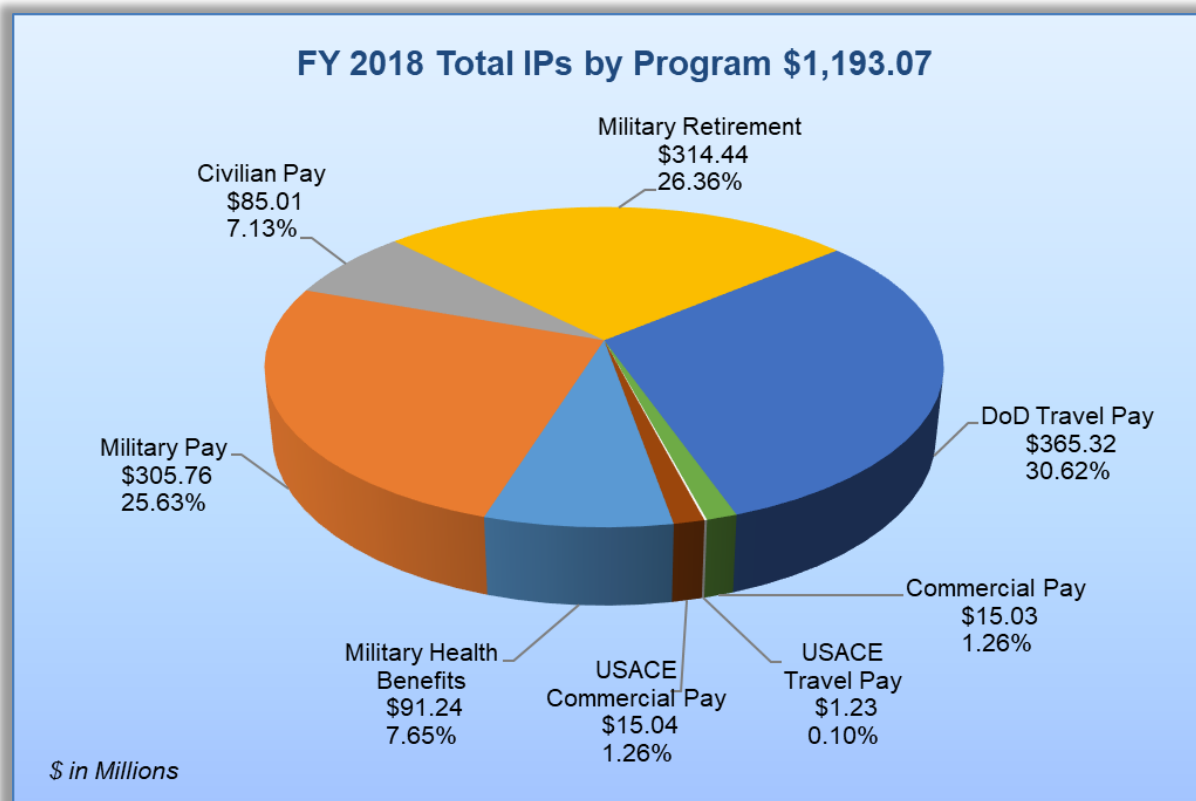
The FY 2018 estimated proper payments presented in Exhibit 9 represent total outlays subject to testing under IPERA (\$574 billion) less estimated improper payments. The estimated improper payments increased from \$957 million in FY 2017 to \$1.2 billion in FY 2018, an increase of \$243 million or 25%. The \$665 million estimated total monetary loss represents the amount that should not have been paid by the Department and in theory should/could be recovered. The \$528 million estimated total non-monetary loss represents the amount that was paid by the Department, but lacked sufficient and/or appropriate supporting documentation or approvals, and did not result in a loss of funds.

In FY 2018, the Department reported improper payments of \$1.2 billion for the following eight programs (see Exhibit 10):

1. Military Health Benefits – Payments made by the Defense Health Agency ([DHA](#)) to private sector contractors for delivery of health care services to [TRICARE](#)–eligible beneficiaries.
2. Military Pay – Payments made by the Defense Finance and Accounting Service ([DFAS](#)) to Active, Reserve, and [National Guard](#) Military 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](#), the [Air Force](#), and the [Marine Corps](#) to Active, Reserve, and National Guard Military Service members and civilian employees for temporary and permanent travel- and/or transportation-related expenses.
6. Commercial Pay – Payments made by DFAS, the Army, and the Navy to vendors and contractors for goods and services. This program does not include payments for “transportation of things” or payments related to government purchase cards.
7. USACE Travel Pay – Payments made by USACE to Active, Reserve, and National Guard Military Service members and civilian employees for temporary and permanent travel- and/or transportation-related expenses.

8. USACE Commercial Pay – Payments made by USACE to vendors and contractors for goods and services.

Exhibit 10. FY 2018 Total Improper Payments Reported by Program



The information reported in this section complies with the guidance provided in OMB Circular No. A-123, Appendix C and OMB [Circular No. A-136](#). This section provides required information that demonstrates the Department's commitment to reducing improper payments. For additional information on improper payments not included in this report, please refer to [PaymentAccuracy.gov](#).

This section reports detailed information on the following improper payment requirements:

- I. Risk Assessment
- II. Payment Reporting
- III. Recapture of Improper Payments Reporting
- IV. Agency Improvement of Payment Accuracy with the Do Not Pay Initiative
- V. Accountability
- VI. Agency Information Systems and Other Infrastructure
- VII. Sampling and Estimation

I. Risk Assessment

OMB Circular No. A-123, Appendix C requires agencies to review all programs and activities and assess their risk for improper payments. Agencies are required to institute a systematic method of reviewing all programs with the end goal of determining whether the programs are or are not susceptible to significant improper payments¹⁰. Improper payment reviews or risk assessments may use qualitative or quantitative methods. If an agency determines that a program or activity is not susceptible to significant improper payments, the agency must re-assess that program's improper payment risk at least once every three years. Conversely, if an agency determines a program to be susceptible to significant improper payments, the agency is required to estimate and report improper payments for that program annually.

Programs already reporting an annual improper payment estimate in accordance with OMB Circular No. A-123, Appendix C requirements do not need to perform an additional improper payment risk assessment to comply with IPERA requirements, as the quantitative risk assessment method used for reporting the annual estimate fulfills the risk assessment requirement under IPERA. In FY 2018, the Department reported improper payment estimates for each of its eight programs. As a result, in FY 2018, the Department was not required to perform additional risk assessment reviews on its programs. However, in subsequent fiscal years, if a new program is identified or established, a risk assessment should be completed after the first 12 months of the program's operation.



¹⁰ "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% of program outlays and \$10 million of all program or activity payments made during the fiscal year reported or (2) \$100 million (regardless of the improper payment percentage of total program outlays).

II. Payment Reporting

Exhibit 11 reports the estimated amount of payments that were properly paid (PP), improperly paid (IP), and the corresponding percentages of each by program for FY 2018. It also reports the estimated amount of improper payments that resulted in overpayments or underpayments in FY 2018 and the OMB-approved future year (i.e., FY 2019) reduction targets by program.

Exhibit 11. FY 2018 Improper Payment Reduction Outlook

(\$ in millions)

Program Name	FY 2018 Outlays	FY 2018 PP Amount	FY 2018 PP Rate (%)	FY 2018 IP Amount	FY 2018 IP Rate (%)	FY 2018 Over-Payment	FY 2018 Under-Payment	FY 2019 Est. Outlays	FY 2019 Est. IP Rate (%)	FY 2019 Est. IP Amount	Month and Year Start Date for Data	Month and Year End Date for Data
Military Health Benefits ^{1, 2, 3}	\$ 23,296.55	\$ 23,205.31	99.61%	\$ 91.24	0.39%	\$ 72.38	\$ 18.86	\$ 24,205.12	0.80%	\$ 193.87	Oct-2016	Sep-2017
Military Pay ⁴	100,285.18	99,979.42	99.70%	305.76	0.30%	288.64	17.12	103,920.24	0.30%	311.76	Aug-2017	Jul-2018
Civilian Pay	61,609.67	61,524.66	99.86%	85.01	0.14%	85.01	-	61,408.83	0.13%	79.83	Aug-2017	Jul-2018
Military Retirement	69,367.74	69,053.30	99.55%	314.44	0.45%	283.32	31.12	60,566.10	0.40%	242.26	Aug-2017	Jul-2018
DoD Travel Pay ^{5, 6, 7, 8}	7,961.95	7,596.63	95.41%	365.32	4.59%	345.79	19.53	11,953.70	5.75%	687.34	Aug-2017	Jul-2018
Commercial Pay ^{9, 10, 11}	292,790.29	292,775.26	99.99%	15.03	0.01%	15.03	-	330,043.97	0.01%	32.92	Jul-2017	Jun-2018
Commercial Bill Pay Office Naples ¹⁰												
USACE Travel Pay	269.98	268.75	99.54%	1.23	0.46%	1.19	0.04	233.01	0.42%	0.99	Jul-2017	Jun-2018
USACE Commercial Pay ^{12, 13}	<u>18,610.93</u>	<u>18,595.89</u>	99.92%	<u>15.04</u>	0.08%	<u>8.89</u>	<u>6.15</u>	<u>19,352.22</u>	0.25%	<u>48.38</u>	Jul-2017	Jun-2018
Total	<u>\$ 574,192.29</u>	<u>\$572,999.22</u>	99.79%	<u>\$ 1,193.07</u>	0.21%	<u>\$ 1,100.25</u>	<u>\$ 92.82</u>	<u>\$ 611,683.19</u>	0.26%	<u>\$ 1,597.35</u>		

Note: Amounts may not sum or calculate exactly due to rounding.

Exhibit 11 Footnotes:

¹ DHA reports data 12 months in arrears. The sample populations for the Military Health Benefits program is comprised of nine sub-programs. 86% of the transactional data samples (outlays) from these sub-programs fall within the period October 2016 to September 2017. The remaining sub-program transactional data samples are for consecutive 12 month periods falling between August 2016 to October 2017.

² FY 2018 outlays are the sum of the dollars paid for civilian health care by private sector contractors to health care providers and/or TRICARE beneficiaries. These payments are reviewed by an external independent contractor (EIC) on a quarterly basis. In addition, the FY 2018 outlays also include administrative payments shared among multiple contractors to administer the TRICARE program and other contracts that are not included in the DHA EIC audits, but which are subject to internal and external pre- and post-payment controls.

³ DHA established its FY 2019 projected IP rate of 0.80% based on a trend of actual improper payments data from prior years. These figures are estimated to be higher than the FY 2018 actuals as a result of DHA's implementation of medical record reviews in FY 2019 (which have the potential to identify additional improper payments), and the implementation of the National Defense Authorization Act ([NDAA for FY 2017](#)) legislative requirements, which established changes to the TRICARE program that could result in increased payment errors.

⁴ The FY 2019 IP rate for the Military Pay program is projected to be 0.30%. This rate remains constant to the IP rate of 0.30% that was estimated and reported in FY 2018. In FY 2019, the Department will implement a revamped sampling plan for this program, which will introduce verification of Military Service member pay and allowances (i.e., entitlements) against existing supporting documentation. The impact of this change on the Department's process of identifying and reporting IPs is unknown. As such, until the results of the new post-payment review procedures conducted in FY 2019 are evaluated, the future year projected IP rate for this program remains constant to the FY 2018 achieved IP rate.

⁵ In FY 2018, the Navy was able to complete 12 months of IPs testing on their FY 2017 Windows Integrated Automated Travel System (WinIATS) travel payments and the Marine Corps was able to complete the remaining four months of IPs testing on their FY 2017 WinIATS travel payments. With these additional testing results, the amounts reported in the DoD AFR for FY 2017 for Outlays, IP Amount, and IP Rate would be revised to: Outlays = \$6,412.23 million, IP Amount = \$368.88 million, and IP Rate = 5.75%. These revised numbers include only nine months of the Defense Travel System data (July 2016 – March 2017).

⁶ The DoD Travel Pay program reports travel payments disbursed for the period August 2017 – July 2018 by DFAS and the Military Services. However, the following Army Outside the Continental United States. (OCONUS) offices used different 12 month sampling timeframes in FY 2018 to test their travel payments: Italy Finance Office (October 2017 – September 2018) and Benelux Finance Office (October 2017 – September 2018). In addition, the Air Force also used a different 12 month sampling timeframe in FY 2018 to test their travel payments (i.e., July 2017 – June 2018).

⁷ The DoD Travel Pay figures reported for FY 2018 do not include data from the Army 266th Financial Management Support Center (FMSC). A new rotational policy in Europe resulted in high turnover in Army 266th FMSC and the FMSC personnel were not able to complete the IP testing for FY 2018. Army 266th FMSC reported the following travel IPs data in FY 2017: Outlays = \$17.49 million, IP Amount = \$0.02 million, and IP Rate = 0.11%.

⁸ The FY 2019 rate for the DoD Travel Pay program is projected to be 5.75%. This rate is 0.25% lower than the target rate of 6% that was projected for FY 2018. Due to drastic fluctuations in the IP rates over the past three fiscal years, the Department is still working to establish a baseline for this program. Moreover, even though numerous corrective actions have been taken to reduce IPs in this program, until a more consistent baseline is established, future year IP target rates will be projected based on the average rates reported for this program in the previous three fiscal years. The average IP rate for this program based on the rates reported in FY 2016, FY 2017, and FY 2018 is 5.86%. As such, the Department is confident that 5.75% is an achievable target rate.

⁹ The Commercial Pay program reports commercial payments disbursed for the period July 2017 – June 2018 by DFAS, the Army, and the Navy. However, the following Army OCONUS offices used different 12 month sampling timeframes in FY 2018 to test their commercial vendor service payments: 175th FMSC (August 2017 – July 2018), Italy Finance Office (October 2017 – September 2018), and Benelux Finance Office (October 2017 – September 2018). Additionally, the figures reported in Exhibit 11 do not include data from the Army 266th FMSC for either FY 2017 or FY 2018. The Commercial Pay program is reported as the DFAS Commercial Pay program on [PaymentAccuracy.gov](https://www.paymentaccuracy.gov).

¹⁰ Effective FY 2018, the Navy Commercial Bill Pay Office Naples was sampled by DFAS and is reported as part of the Commercial Pay program.

¹¹ The Commercial Pay program is comprised of payments made by DFAS, the Army, and the Navy to vendors and contractors for goods and services. This program does not include payments for “transportation of things” or payments related to government purchase cards. Title 31, United States Code, section 3726 ([31 U.S.C. §3726](#)) gives the General Services Agency ([GSA](#)) the authority and responsibility to audit and settle all federal payments for transportation. The [GSA Transportation Audits Division](#) conducts post-payment audits on all transportation payments (and supporting documentation) provided by the Department. GSA reviews DoD transportation payments for overcharges only. GSA finances their post-payment audit contract and audit-related functions with overpayments collected from the transportation payments previously paid by the Department and other federal agencies. GSA reported the following data related to DoD transportation payments for the months July 2017 – June 2018: Total Number of Transactions Submitted by the Department = 15.32 million, Total Value of Transactions Submitted by the Department = \$4,083.03 million, Total Number of Overcharges Collected by GSA = 0.43 million, and Total Value of Overcharges Collected by GSA = \$9.32 million.

¹² In FY 2018, USACE was able to complete the remaining 6 months of IPs testing on their FY 2017 commercial payments. With these additional testing results, the amounts reported in the DoD AFR for FY 2017 for Outlays, IP Amount, and IP Rate would be revised to: Outlays = \$17,128.35 million, IP Amount = \$157.87 million, and IP Rate = 0.92%.

¹³ The FY 2019 Estimated IP rate of 0.25% for USACE Commercial Pay is an increase over the 0.08% reported in FY 2018 (which represents the calculated rate based on estimated IPs as a percent of total FY 2018 outlays). The increase is due to receipt of significant supplemental funding, resulting in increased risk of improper payments associated with a high volume of contract actions occurring in dispersed locations, some remote, under tightened deadlines.

Exhibit 12 reports the amount of FY 2018 improper payments identified in samples by program that resulted in actual monetary losses to the Department. These statistically-based sample amounts are then extrapolated to the payment population of the program to calculate an estimate of the monetary loss to the Department due to improper payments by program. Monetary loss to the Department would be an amount that should not have been paid and, in theory, should/could be recovered. This table excludes payments classified as improper payments solely on the basis of insufficient supporting documentation, since these payments do not represent an actual monetary loss.

Exhibit 12. FY 2018 Improper Payment Classification (Monetary Loss)

(\$ in millions)

Program Name	Actual Monetary Loss to the Department Identified in the Sample*	Estimated Total Monetary Loss to the Department *
Military Health Benefits	\$ 4.14	\$ 72.38
Military Pay	276.66	288.64
Civilian Pay	85.01	85.01
Military Retirement	76.24	76.45
DoD Travel Pay	1.98	126.16
Commercial Pay	0.60	15.03
USACE Travel Pay	0.03	1.19
USACE Commercial Pay	-	-
Total	\$ 444.66	\$ 664.86

* The monetary loss amounts reported in Exhibit 12 will not match the overpayments reported in Exhibit 11, which include both monetary and non-monetary improper payments.



A waterspout forms as the USS Gerald R. Ford travels in the Atlantic Ocean, Dec. 4, 2017. The aircraft carrier is underway conducting test and evaluation operations.

Navy photo by Petty Officer 2nd Class Martin Widenhouse

Exhibit 13 reports the root causes for overpayments and underpayments by amount and program for FY 2018.

Exhibit 13. FY 2018 Improper Payment Root Cause Category Matrix

(\$ in millions)

Program Name	Payment Type	Inability to Authenticate Eligibility: Inability to Access Data	Administrative or Process Errors Made by the Department	Administrative or Process Errors Made by Other Parties ¹	Medical Necessity	Insufficient Documentation to Determine	Notification of Death After Monthly Payments Disbursed for Military Retirees and Annuitants	Total
Military Health Benefits	Overpayments	\$ 0.02		\$ 71.97	\$ 0.18	\$ 0.21		\$ 72.38
Military Health Benefits	Underpayments			18.86				18.86
Military Pay ²	Overpayments		288.64					288.64
Military Pay ²	Underpayments		17.12					17.12
Civilian Pay	Overpayments		85.01					85.01
Civilian Pay	Underpayments							-
Military Retirement ²	Overpayments		207.22				76.10	283.32
Military Retirement ²	Underpayments		31.12					31.12
DoD Travel Pay ²	Overpayments		125.42			220.37		345.79
DoD Travel Pay ²	Underpayments		19.53					19.53
Commercial Pay	Overpayments		15.03					15.03
Commercial Pay	Underpayments							-
USACE Travel Pay	Overpayments		1.19					1.19
USACE Travel Pay	Underpayments		0.04					0.04
USACE Commercial Pay	Overpayments		8.89					8.89
USACE Commercial Pay	Underpayments		6.15					6.15
Total		\$ 0.02	\$ 805.36	\$ 90.83	\$ 0.18	\$ 220.58	\$ 76.10	\$ 1,193.07

Exhibit 13 Footnotes:

¹ “Other Parties” includes Participating Lenders, Health Care Providers, or any other organizations administering federal dollars.

² The Military Pay, Military Retirement, and DoD Travel Pay programs were determined to be susceptible to significant improper payments in accordance with OMB Circular No. A-123, Appendix C.

Root Causes and Corrective Action Plans for Programs Susceptible to Significant Improper Payments (IPs Exceeding \$100 million)

When significant improper payments are identified in a program through testing, DoD Components are required to determine the root causes of the improper payments and to develop CAPs to remediate them. The CAPs for the applicable program are monitored throughout the year by DoD Components and the Office of the Under Secretary of Defense (Comptroller) ([OUSD\(C\)](#)) to ensure milestone dates for corrective actions are completed on a timely basis. The implementation and effectiveness of corrective actions is evidenced through the subsequent improper payment testing results for the program. Based on testing performed on the eight programs in FY 2018, three programs (Military Pay, Military Retirement, and DoD Travel Pay) were estimated to have made improper payments in excess of \$100 million and were therefore required to develop CAPs and disclose them in this report. In addition, during FY 2018, OUSD(C) worked with DoD Components to strengthen the CAPs for these programs by performing in-depth assessments to ensure that the corrective actions identified were measurable, timely, and effective.

The following information related to improper overpayments and underpayments identified through testing, as well as root causes and corrective actions, is summarized and described at the DoD consolidated level. Individual DoD Component CAPs and target completion dates are maintained and monitored by the DoD Components and OUSD(C). Generally, corrective actions are developed and executed by individual DoD Components with oversight provided by OUSD(C).



Military Pay

In FY 2018, the estimated improper payments for the Military Pay program were \$306 million, approximately 94.40% of which were identified as overpayments (see Exhibit 14). Of those overpayments, the majority resulted from debts established after Military Service members left the Department and/or debts initiated and recorded within the military pay systems for Active and Reserve Component Military Service members. This estimate was based on a sampling methodology with a 95% confidence interval, which equated to a 0.30 (+/- 0.02)% improper payment rate and an estimated proper processing rate of 99.70%.

Exhibit 14. FY 2018 Military Pay Estimated Improper Payments by OMB Root Cause Category

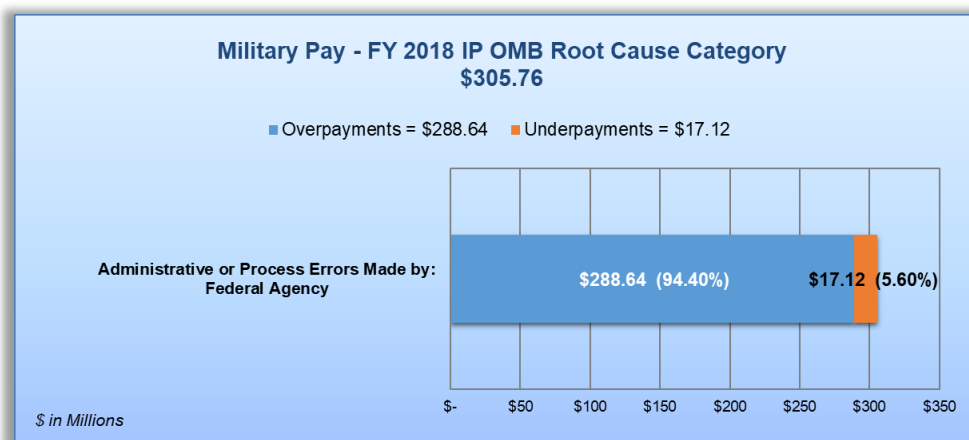
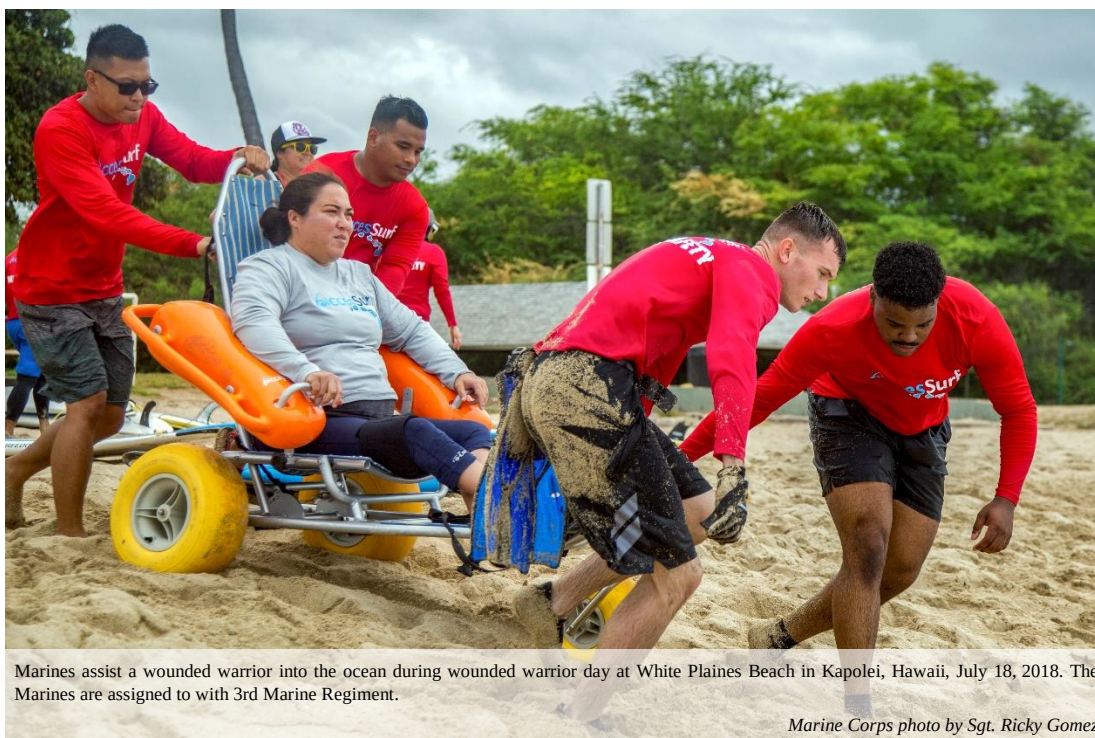


Exhibit 15. Military Pay Summary Corrective Action Plans

The root cause for all improper payments in the Military Pay program was attributed to Administrative or Process Errors Made by the Department, which accounted for \$306 million, or 100%, of the improper payments.

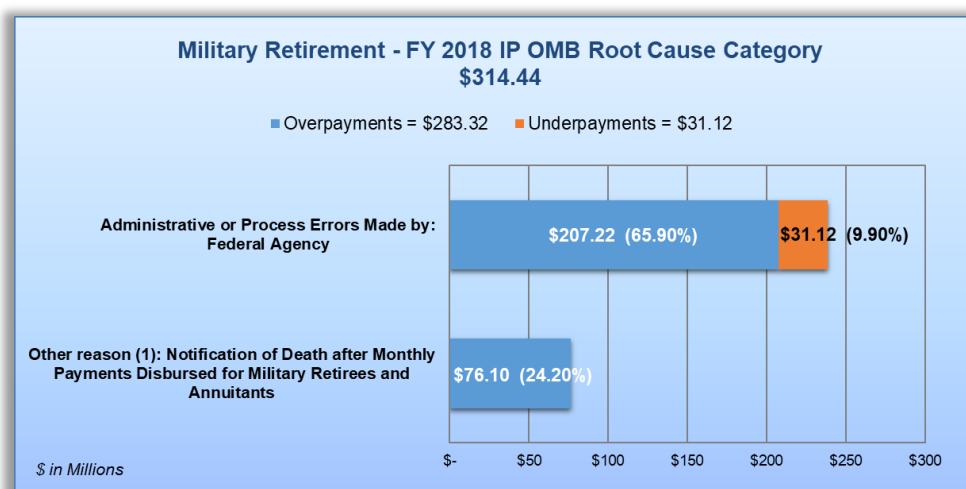
Improper Payment Root Cause Category	Corrective Actions	Target Completion Date
<u>Administrative or Process Errors Made by the Department</u> Contributing factors can include payroll data input errors and untimely updates to payroll records and systems.	- For improper payment statistical sample selections, obtain sufficient personnel supporting documentation for the payroll disbursement from the relevant DoD Component. - Based on review of supporting documentation for each sample item, determine improper payment exceptions and report exceptions to the relevant DoD Component. - Provide instructions to relevant DoD Components for preparation of a root cause analysis for each improper payment exception. Instructions will include guidance for summary level reporting to leadership. - Relevant DoD Components will develop corrective action plans to address specific root causes identified for improper payments attributable to their payroll disbursements. - Based on the root cause analysis, training will be developed and delivered to improve effectiveness over manual payroll processing controls. - Evaluate the cost/benefit of additional or enhanced system controls over payroll processing and implement as applicable.	September 2019



Military Retirement

In FY 2018, the estimated improper payments for the Military Retirement program were \$314 million. Approximately 90.10% of these improper payments were identified as overpayments (see Exhibit 16). This estimate was based on a sampling methodology with a 95% confidence interval, which equated to a 0.45 (+/- 0.10)% improper payment rate and an estimated proper processing rate of 99.55%.

Exhibit 16. FY 2018 Military Retirement Estimated Improper Payments by OMB Root Cause Category



The primary root cause for improper payments in the Military Retirement program was attributed to Administrative or Process Errors Made by the Department, which accounted for \$238 million, or 75.80%, of the program's improper payments. The second major root cause for improper payments in the Military Retirement was Notification of Death after Monthly Payments Disbursed for Military Retirees and Annuitants, which accounted for \$76 million, or 24.20%, of the program's improper payments.

Exhibit 17. Military Retirement Summary Corrective Action Plans

Improper Payment Root Cause Category	Corrective Actions	Target Completion Date
<u>Administrative or Process Errors Made by the Department</u>		
- Processing errors were noted for retired and annuitant pay: new annuitants, new retirees, and changed annuitant account, which included: - Payments made despite insufficient documentation, - Errors in following processing procedures and applying policy changes for Department of Veterans Affairs waivers awards - Untimely application of Dependency and Indemnity Compensation offsets - Systematic computation errors - Manual computation errors	- Revise the Military Retirement Sampling Plan to stratify the population by risk level based on account type: new retiree accounts, new annuitant accounts, changed retiree accounts, changed annuitant accounts, unchanged retiree accounts, and unchanged annuitant accounts. This sampling approach is designed to provide greater sample coverage and insight into each of the categories where processing errors were noted. - Conduct bi-monthly workgroup meetings to provide DFAS leadership with timely, detailed information to assist in identifying predominant error types, root causes, suggested corrective actions and other data grouped by account type. This includes detailed error descriptions. The information disseminated to DFAS leadership will be used by them to better manage the military retirement program and minimize improper payments. - Increase the scope and frequency of retired and annuitant operations internal personnel training. Training will be focused on the trends identified in the post pay review deliverables.	November 2020
<u>Notification of Death After Monthly Payments Disbursed for Military Retirees and Annuitants</u>		
Improper payments were made to deceased retirees and annuitants because the notification of death was not obtained until after the monthly payments were disbursed	- Validate the existence of the retiree/annuitant, if living outside the United States. - Certify annually the existence and entitlement for all annuitants who: - Are under 55 years of age, - Receive hard copy checks in a foreign country, and - Have a permanent disability (regardless of age). - Conduct periodic, random certifications for retirees over a certain age. - Validate military retiree's existence if payments are returned and/or if a benefit account was suspended for several months due to bad check/correspondence address.	Completed in FY 2018

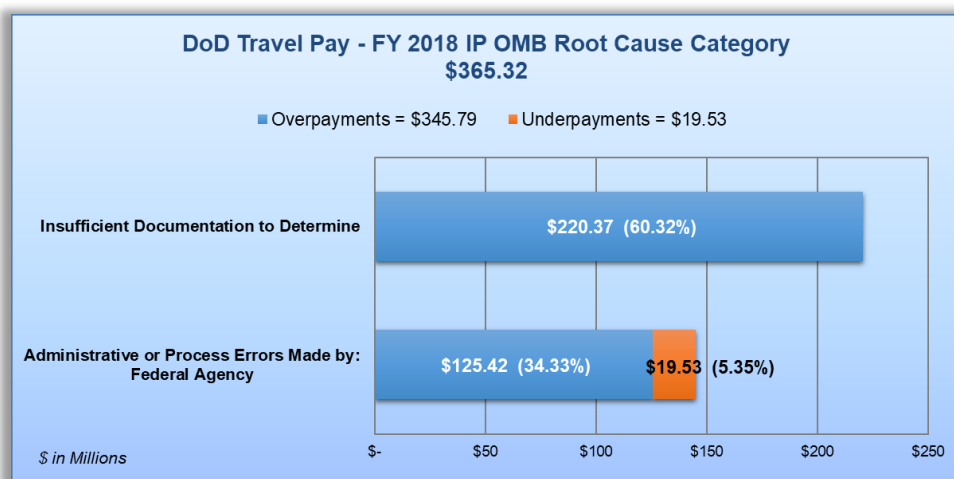


DoD Travel Pay

In FY 2018, the estimated improper payments for the DoD Travel Pay program were \$365 million. Approximately 94.65% of these improper payments were identified as overpayments (see Exhibit 18). This estimate was based on a sampling methodology with a 95% confidence interval, which equated to a 4.59 (+/- 0.43)% improper payment rate and an estimated proper processing rate of 95.41%.

Payments for the DoD Travel Pay program were processed through three travel systems: the Defense Travel System ([DTS](#)), the Windows Integrated Automated Travel System (WinIATS), and the Air Force's Reserve Travel System (RTS). The largest portion of travel payments are processed through DTS.

Exhibit 18. FY 2018 Travel Pay Estimated Improper Payments by OMB Root Cause Category



The primary root cause for improper payments in the DoD Travel Pay program was attributed to Insufficient Documentation to Determine, which accounted for \$220 million, or 60.32%, of the program's improper payments. The second major root cause for improper payments in the DoD Travel Pay program was Administrative or Process Errors Made by the Department, which accounted for \$145 million, or 39.68%, of the program's improper payments.

Exhibit 19. DoD Travel Pay Summary Corrective Action Plans

Improper Payment Root Cause Category	Corrective Actions	Target Completion Date
<u>Insufficient Documentation to Determine</u>		
Root cause of improper payments are not always clearly defined or linked to a DoD Component's corrective action plans.	Provide additional guidance and templates to assist DoD Components in documenting root cause and corrective actions.	December 2018
Lack of sampling plan and/or execution of sampling plan and testing	- Sampling plans will be prepared and documented using approved templates with site specific modifications as necessary. Sampling plans will be prepared for all locations and travel pay systems as applicable and will include a full 12 months of samples. - Sampling plans will be reviewed by DFAS statisticians to ensure compliance with OMB guidelines prior to execution.	December 2018
Lack of process to evaluate, monitor, and measure improper payments noted in sample testing and the related corrective actions	- Develop and implement processes and tools to evaluate, monitor, and measure improper payments for DoD Travel Pay, including: - Develop performance metrics and track via spreadsheets and database dashboards, - Perform periodic quality assurance reviews over metrics and corrective action implementation, and - Monitor recovery of improper overpayments. - Develop and publish guidance to DoD Components establishing a monthly reporting schedule for sampling and testing and gaining efficiency in sample reviews.	December 2018 Completed October 2017
<u>Administrative or Process Errors Made by the Department</u>		
The following types of improper payments result from administrative or process errors: - Overpayment of travel advances, - Airfare paid incorrectly, - Travelers reimbursed for expenses with missing or invalid receipts, and - Travel vouchers paid without the proper signature.	- Develop and deliver focused training for: - Validating the status of previous advances before disbursing another advance; - Computing cost comparisons for travel reimbursements; - The roles of authorizing officials and reviewers in reviewing receipts prior to their approval signature; and - Incorporate the DoD video on improper payments, including missing/invalid receipts, into personnel required training programs. - Develop and implement standard checklists to be used in travel voucher reviews to assess the completeness and accuracy of the travel payment prior to disbursement.	December 2018

III. Recapture of Improper Payments Reporting

The Department performs three separate and distinct activities which can result in the collection of amounts improperly paid to the recipient. Collection of these amounts is often referred to as “payment recapture.” The three activities performed by DoD are:

- (1) Testing payments selected in statistical samples under OMB Circular No. A-123, Appendix C (IPERA Testing);
- (2) Testing under the requirements of OMB Circular No. A-123 (Enterprise Risk Management and Internal Control Program (ERM/ICP) Control Activities); and
- (3) Payment Recapture Audits as defined under OMB Circular No. A-123, Appendix C (Payment Recapture Audit).

IPERA Testing

Under IPERA Testing, sampled items are tested to identify overpayments or underpayments to eligible recipients, payments to ineligible recipients, payments for ineligible goods or services, and payments for goods or services not received. Tests include review of supporting documentation and such other test procedures as applicable. When a review is unable to discern whether a payment was proper as a result of insufficient or lack of documentation, the payment is considered to be improper.

As part of the Department’s overall system of internal control, individual overpayments identified in sampled items are reported to the DoD Component where the transaction originated. For example, if DFAS were performing the IPERA testing for the DoD Travel Pay program and identified an overpayment involving an Army employee, DFAS would report the overpayment to the Army. The Army would then contact the affected employee and agree upon a repayment method consistent with the Army’s debt management program. In most situations, the repayment would occur through payroll deduction or direct reimbursement by the employee to the Department for the overpayment.

ERM/ICP Control Activities

The framework of internal controls has five components – Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring. Within this framework, Control Activities are the actions management establishes through policies and procedures to achieve objectives and respond to risks in the system of internal control.

Execution of Control Activities can result in the identification of an overpayment. For example, an overpayment in the Commercial Pay program may be identified through Control Activities at the DoD Component level. These overpayments would be subject to collection efforts coordinated between DFAS and the DoD Component offices responsible for originating the transactions. These collections efforts may include direct collection from the contractor or offset against the same contract with that contractor.

Payment Recapture Audit

A Payment Recapture Audit is a review and analysis of a program’s accounting and financial records, supporting documentation, and other pertinent information supporting its payments, and is specifically designed to identify overpayments. It is not an audit in the traditional sense covered by Generally Accepted Government Auditing Standards.

As part of their internal controls over payments, federal agencies are required to conduct Payment Recapture Audits for all programs that expend more than \$1 million in a fiscal year if conducting such audits is cost-effective. However, federal agencies may exclude program payments from Payment

Recapture Audits if the agency determines that Payment Recapture Audits are not a cost-effective method for identifying and recapturing payments. The Department has determined that Payment Recapture Audits are not a cost-effective repayment capture method for its programs, with the exception of a portion of the DoD Travel Pay program administered by the Defense Travel Management Office ([DTMO](#)).

Currently, the only payment recapture audit performed by the Department is conducted by DTMO as part of the DoD Travel Pay program. DTMO reviews all travel vouchers for temporary duty personnel processed through DTS using a set of 14 predefined queries designed to identify the most common improper payments.

Individual overpayments identified by DTMO through its [Travel Policy Compliance Tool](#) are reported through automated notifications to locally based Compliance Tool Administrators at the DoD Component where the travel transaction originated. The DoD Component then contacts the affected employee and agrees upon a repayment method consistent with the DoD Component's debt management program. In most situations, the repayment occurs through payroll deduction or direct reimbursement by the employee to the Department for the overpayment.



[Overpayment Capture Reporting](#)

Exhibit 20 reports the results of overpayments recaptured as a result of IPERA Testing and ERM/ICP Control Activities as “Overpayments Recaptured Outside of Payment Recapture Audits”; overpayments recaptured as a result of Payment Recapture Audit are reported as “Overpayments Recaptured Through Payment Recapture Audits.”

Amounts reported as “Overpayments Recaptured Outside of Payment Recapture Audits” in Exhibit 20 may differ from those reported on Exhibit 11 as “FY 2018 Overpayments” due to: timing differences in reporting, the fact that Exhibit 11 reflects estimates while Exhibit 20 reflects actuals, as well as differences in the manner of compilation. Additionally, note that overpayments identified in one fiscal year may be collected in that fiscal year or in a subsequent fiscal year.

Exhibit 20. FY 2018 Payment Recapture Audit Reporting

(\$ in millions)

Includes Funds Recaptured from a High Priority Program? (Y/N) ¹	Program	Overpayments Recaptured Through Payment Recapture Audits				Overpayments Recaptured Outside of Payment Recapture Audits	
		Amount Identified in FY 2018	Amount Recaptured in FY 2018	Recapture Rate in FY 2018 (%)	FY 2019 Recapture Rate Target (%)	Amount Identified in FY 2018	Amount Recaptured in FY 2018
N	Military Health Benefits ^{2, 3, 4}					\$ 4.14	\$ 22.48
N	Military Pay ⁵					276.66	238.40
N	Civilian Pay ⁵					85.01	85.01
N	Military Retirement ⁶					19.62	17.84
N	DoD Travel Pay ^{7, 8, 9}	\$ 15.67	\$ 11.65	74%	85%	3.69	0.87
N	Commercial Pay					0.01	0.01
N	USACE Travel Pay					1.49	1.28
N	USACE Commercial Pay					10.95	8.65
	Total	\$ 15.67	\$ 11.65	74%	85%	\$ 401.57	\$ 374.54

Exhibit 20 Footnotes:

¹ The threshold for designation as a high-priority program for FY 2018 reporting is \$2 billion in estimated improper payments reported by the federal agency, regardless of the improper payment rate estimate.

² “Amount Identified in FY 2018” represents the total overpayment dollars from sampled claims.

³ These numbers include recoupments for overpayments identified in reviews conducted by an external independent contractor as well as refunds occurring in the course of routine claim adjustments (for claims initially paid in FY 2017 and other fiscal years). DHA has no way to distinguish overpayment recoupments from routine claim adjustments.

⁴ The amount recaptured in FY 2018 for the Active Duty Dental Program ([ADDP](#)) represents refunds shown on contractor invoices to DHA. ADDP data is not included in the TRICARE Encounter Data ([TED](#)) system, thus contractor invoices were used because TED transactions are not available.

⁵ The Military Pay program includes both in-service collections (i.e., collections from active employees) and out-of-service debts (i.e., collections from individuals not actively employed by the Department) in the Amount Recaptured. The Civilian Pay program includes only in-service collections in the Amount Recaptured.

⁶ The amounts identified and recaptured for the Military Retirement program are based on a 100% review of deceased retired and deceased annuitant accounts.

⁷ “Overpayments Recaptured Outside of Payment Recapture Audits” for the DoD Travel Pay program are overpayments of paid DTS and Navy WinIATS vouchers that were identified by DFAS through their sampling and post-payment review process.

⁸ The DoD Travel Policy Compliance Program is the only formal payment recapture audit program of the DoD Travel Pay program and its results are reported “through” payment recapture audits. Program scope is 100% of temporary duty vouchers processed in the DTS and currently includes 14 queries that identify common improper payments.

⁹ “Amount Recaptured” includes debts that have been fully collected or are currently in the debt process, such as payroll deductions.

Exhibit 21 reports the disposition of funds recaptured as a result of Payment Recapture Audits. In accordance with IPERA requirements, only funding which is expired at the time of collection can be reallocated.

Exhibit 21. FY 2018 Disposition of Funds Recaptured Through Payment Recapture Audits

(\$ in millions)

Program	Amount Recaptured *	DoD Expenses to Administer the Program	Payment Recapture Auditor Fees	Financial Management Improvement Activities	Original Purpose	Office of the Inspector General	Returned to the Treasury	Other **
DoD Travel Pay	\$ 11.65	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 11.65
Total	\$ 11.65	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 11.65

* "Amount Recaptured" will be identical to the "Amount Recaptured Through Payment Recapture Audits" in Exhibit 20.

** "Other" funds remain in the original account until cancelled.

Exhibit 22 reports an aging schedule of the amount of overpayments identified through Payment Recapture Audits that are outstanding (i.e., overpayments that have been identified, but not recaptured). Identified overpayments were determined to be uncollectible for one of the following reasons: the amount of the debt is \$10 or less, a waiver has been approved, or the amount is an out-of-service debt (i.e., debt from an individual not actively employed by the Department).

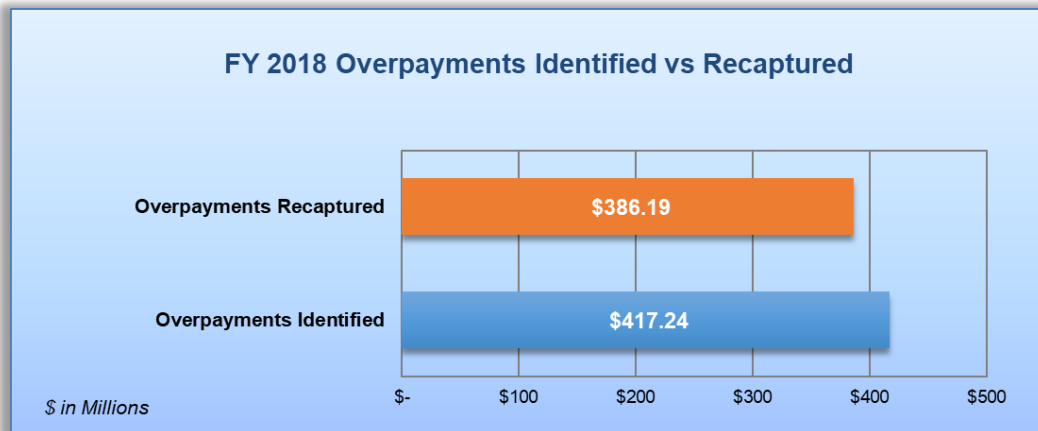
Exhibit 22. Aging of Outstanding Overpayments Identified Through Payment Recapture Audits

(\$ in millions)

Program	Amount Outstanding (0 - 6 months)	Amount Outstanding (6 months - 1 year)	Amount Outstanding (over 1 year)	Amount Determined to Not Be Collectible
DoD Travel Pay	\$ 0.65	\$ 3.24	\$ 0.12	\$ 0.01
Total	\$ 0.65	\$ 3.24	\$ 0.12	\$ 0.01

Exhibit 23 reports the actual amount (i.e., not estimated) of overpayments identified in FY 2018 and the actual amount of overpayments recaptured in FY 2018. Note: not all overpayments will be collected in the same fiscal year that they were made and/or identified. The Department continues to work to improve its methods to identify, collect, and report improper payments.

Exhibit 23. FY 2018 Overpayments Identified and Recaptured



IV. Agency Improvement of Payment Accuracy with the Do Not Pay Initiative

The Department of Treasury ([Treasury](#)) Do Not Pay ([DNP](#)) Portal is the legislatively-mandated and OMB-designated source of centralized data and analytics services to help federal agencies verify eligibility for payment and to identify and prevent fraud, waste, and abuse associated with improper payments. Federal agencies interface with Treasury's centralized data to achieve a higher degree of certainty that a payee is legitimate and eligible before making a payment. All payments that are identified to be potentially improper are then adjudicated and either paid or not paid. Improper payments, however, may still occur at some later point due to reasons that the DNP Portal cannot detect or prevent.

[DFAS](#)

DFAS sends a Commercial Pay weekly batch file of invoices in a non-pay status to the DNP Portal and receives results the next day. DFAS then researches any potential improper payments identified to determine if the proposed payment is proper based on established business rules. To date, DFAS has been able to adjudicate and clear all potential improper payments identified using the DNP Portal.

DFAS does not conduct payment reconciliations to the Debt Check database, which is subset of the data contained in the [Treasury Offset Program](#), and the Credit Alert Verification Reporting System ([CAIVRS](#)). 99% of the false positives received are based on the Death Master File ([DMF](#)) results along with name match results from the DNP Portal. The remaining 1% of false positives are deemed not to be improper payments based on established business rules related to vendor performance in accordance with established contracts.

[DHA](#)

Individual Payments

DHA processes relatively few (5 – 20) case recoupment refunds each month for small dollar amounts (\$5 – 20,000). The DNP Portal search is utilized for 100% of all case recoupment refunds prior to making the payment to verify (1) a business or individual has not been placed on the List of Excluded Individuals/Entities ([LEIE](#)) and/or (2) an individual is not deceased. Any matches are referred to the DHA Office of General Counsel ([DHA OGC](#)).

Vendor, Contract Payments

DHA processes an average of 225 routine payments per month for 13 unique contractor payees. Those unique contractor Employer Identification Numbers (EINs) are checked in the DNP Portal only once at the beginning of each month. The initial DNP Portal check is then carried for all remaining payments being made to that unique payee for the rest of the month. This process is then repeated every month, therefore maintaining 100% validation of a contractor in the DNP Portal. This pre-payment validation of payees is to verify that a DHA payee has not been placed on the System for Award Management ([SAM](#)) Exclusion Records (referred to as the Excluded Parties List System (EPLS) in IPERIA) or the LEIE. Any matches are validated with the Treasury Offset Program, ensuring the contractor does not have the same EIN as an individual's Social Security Number. The contractor is responsible for resolving these matching issues due to proprietary reasons. If the contractor is on the SAM, LEIE, and/or Treasury Offset Program list, the finding is referred to the assigned Contracting Officer.

The risk for payments to a subcontractor or individual via the contractor, however, lies outside of DHA control. DHA contractors are not required to utilize the DNP Portal and there is no current mechanism in place to require the contractors to use the DNP Portal at the pre-payment phase to comply with IPERA requirements.



[USACE](#)

On a daily basis, USACE sends payments certified for the next day's disbursing process to the DNP Portal. The DNP Portal searches for potential matches of pending USACE payments and vendors/persons identified on the DMF and the SAM Exclusion Records. USACE then researches any potential improper payments identified to determine if the proposed payment is proper based on established business rules. To date, USACE has been able to adjudicate and clear all potential improper payments identified using the DNP Portal.

USACE has determined that the majority of matches received were false positives. The other matches received were not deemed to be improper payments based on established business rules related to vendor performance in accordance with established contracts.

[File Matching with the DMF Outside of Do Not Pay for Military Retiree and Annuitant Benefit Payments](#)

The Defense Manpower Data Center ([DMDC](#)) has a computer matching agreement with the Social Security Administration ([SSA](#)) to use its DMF to identify potential accounts that need to be suspended or cancelled as a result of a retiree's or annuitant's passing. As part of the end-of-month processing, DFAS produces two files (one for retirees, one for annuitants) that are sent to DMDC to match or conduct comparisons against the monthly DMF. The results are compiled and forwarded to DFAS.

DFAS then runs its match process to suspend (but not cancel) pay accounts and to notify next of kin that this action was based on information received from SSA. The disbursement system suspends payment to prevent additional benefits from being improperly paid. For any electronic funds transfer payment that was mistakenly disbursed, an electronic transaction is generated to automatically reclaim the payment from the bank account where it was originally deposited after the official notification of death is processed. The normal recovery rate is approximately 95% within 60 days of the official death confirmation.

V. Accountability

The Department recognizes the difficulty of any single official exercising direct personal control over all aspects of each business transaction. Therefore, the Department relies on automated systems, manual controls, and accountable officials to ensure accountability of government funds, including the accuracy, propriety, and legality of payments. The Under Secretary of Defense (Comptroller)/Chief Financial Officer ([USD\(C\)/CFO](#)) is the Accountable Official for the Department and is responsible for ensuring that, to the greatest extent possible, all DoD payments are accurate.

The Department adheres to [10 U.S.C. §2773\(a\)](#), which holds Departmental Accountable Officials (DAOs) and Certifying Officials (COs) accountable for government funds. DAOs and COs 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](#), which addresses the selection, appointment, responsibilities, and qualifications for certifying officers; certification of vouchers for payment; DAOs; random review of disbursement vouchers; and pecuniary liability. Moreover, the Department's efforts to recover overpayments are administered in accordance with the debt collection policy in DoD FMR, [Volume 16](#).

The DoD FMR also contains chapters that specifically address improper payments (i.e., [Volume 4, Chapter 14](#)) and recovery auditing (i.e., [Volume 10, Chapter 22](#)). The Deputy Chief Financial Officer ([DCFO](#)) is the Executive Agent and Senior Accountable Official (SAO) for the DoD Payment Integrity Program. The DCFO, along with the Director of Accounting and Finance Policy and the Payment Integrity Program manager, provides oversight to the Payment Integrity Program and are each held accountable in their performance plans for reducing and recapturing improper payments as well as achieving compliance with IPERA.

The Department continues to take many proactive steps to hold individuals accountable for the prevention and reduction of improper payments. In FY 2013, following the DoD Travel Pay program's initial year of noncompliance, a Department-wide remediation plan was developed and implemented to assist the program in meeting its future years' improper payment target rates. By FY 2017 this plan evolved into an improper payments SAO steering committee, which is responsible for proactive oversight of the Payment Integrity Program, implementing best practices, monitoring performance, and driving actions for achieving IPERA compliance. This committee, which is comprised of SAOs from across the Military Services and several other DoD Components, is held accountable for reducing and recapturing improper payments through corrective action plans and remediation progress is monitored and measured through performance metrics. Moreover, the SAO steering committee helps ensure that improper payment estimates for all programs are complete and accurate and that program target rates are met.

[Military Pay](#)

The Department is committed to ensuring that Military Service members are paid timely and accurately. To accomplish this important mission, individuals within the Military Pay hire-to-rotate process are held accountable for their respective areas of responsibilities. Military Service members are held accountable to report timely their eligibility information as well as any qualifying change of life situations affecting their pay to their Personnel and/or Finance offices. Personnel and/or Finance offices are held accountable to process Military Service member payroll and benefit documentation accurately and timely and to ensure the documentation is correctly entered into entitlement systems. Personnel and/or Finance office employees are required to perform reconciliations on a regular basis and to make timely edits or updates to a Military Service member's pay in entitlement systems, as necessary. Management is held accountable for ensuring that controls are in place to properly capture, record, and approve Military Service

members' pay and entitlement information. Additionally, management is responsible for reviewing finance reports, which reflect pay and entitlements paid to Military Service members, and for conducting monthly internal reviews to compare and reconcile pay and personnel records.

Military Retirement

The DFAS Director of Retired and Annuitant [\(R&A\) Pay](#) is held accountable in a performance plan for reducing and recapturing improper payments. The DFAS Director of R&A Pay is required, under a performance plan element of "Internal Controls and Audit Support," to actively support R&A work group efforts to reduce improper payments identified by the DFAS Post-pay Review & Analysis, Reports & Analysis Enterprise Solutions & Standards – Compliance team. Moreover, executives at [DFAS Cleveland](#), where R&A Pay is managed, are held accountable to meet established percentage goals for improper payments through annual performance plan criteria.

DoD Travel Pay

The Department is committed to ensuring that all employees, both Military Service members and civilians, are reimbursed timely and accurately for their travel-related expenses. To accomplish this mission, individuals within the travel management process are held accountable for their respective areas of responsibility.

DAOs involved in the travel management process serve as control points within the Department. Individuals officially appointed as DAOs for the travel process may include reviewing officials, approving officials, and authorizing officials. If appointed, DAOs are subject to pecuniary liability for illegal, improper, or incorrect payments resulting from information, data, or services they negligently provide to COs and upon which the COs relied to certify payment vouchers. DAOs must be appointed and terminated using a DoD (DD) Form 577.

COs are subject to pecuniary liability under 10 U.S.C. §2773(a) and [31 U.S.C. §3528](#). They are responsible for certifying travel claims for payment, forwarding certified claims to the supporting disbursing office, comparing pre-trip and post-trip estimates of expenses, reviewing all lodging receipts, and reviewing individual reimbursable expense receipts of \$75 or more. Responsibilities for individuals appointed as COs are applicable to both DTS and non-DTS travel claims. COs must be appointed by an appropriate authority and they must acknowledge their appointment as a CO by signature as well as complete a DD Form 577.

Travelers are held accountable for preparing their vouchers (i.e., DD Form 1351-2) after travel has been completed. Travelers must provide all supporting documentation including the original (or legible copies of) orders and receipts for all lodging expenses, as well as claimed reimbursable expenses of \$75 or more, to their DAOs and/or COs. Moreover, travelers are liable under [18 U.S.C. §§287](#) and [1001](#) and the False Claims Act, [31 U.S.C. §§3729-3731](#), if they knowingly submit false, fictitious, or fraudulent travel claims.

VI. Agency Information Systems and Other Infrastructure

Military Pay

Internal Controls

The Department has internal controls in place that support the reduction of improper payments in the Military Pay program to the levels the Department has targeted. However, in FY 2018 there were three outstanding material weaknesses in the Military Pay hire-to-rotate process. The material weaknesses were identified by the Army and the Navy in FY 2011. Although the material weaknesses have had an impact on the Payment Integrity Program, significant progress has been made by the Army and the Navy to remediate them. The Army and the Navy plan to fully resolve the deficiencies by FY 2020. Moreover, OUSD(C) provides ongoing oversight to ensure that the material weaknesses are resolved by their target dates and coordination continues between the ERM/ICP and the Payment Integrity Program.

Human Capital

Currently, the Department has the human capital it needs to reduce improper payments in the Military Pay program to the levels the Department has targeted. However, as the Military Pay program evolves and DoD operations change, additional skill sets and personnel resources may be needed to sustain and advance the program.

Information Systems and Other Infrastructure

The Department has the information systems and other infrastructure it needs to reduce improper payments in the Military Pay program to the levels the Department has targeted. The primary system currently used by the Department to process Military Pay is the Defense Joint Military Pay System (DJMS). DJMS received an unmodified System and Organizational Control (SOC) 1 Type 2 report under Statement on Standards for Attestation Engagements ([*SSAE* No. 18](#)) in FY 2018. However, as technology advances, the Department continues to consider ways to improve the accuracy and efficiency of Military Pay through implementation of new payroll and entitlement processing systems and enhancements to existing systems.

Military Retirement

Internal Controls

The Department has internal controls in place to support the reduction of improper payments in the Military Retirement program to the levels the Department has targeted. As part of the internal control framework for this program, the DFAS Director of R&A Pay has identified and documented known risks associated with the processes for providing pay services to the customers of the Military Retirement program. Along with identifying these risks by process, the Director of R&A Pay instituted key controls and control activities to mitigate the documented risks. The Director also tests the controls to ensure their effectiveness and documents the test results. In addition, OUSD(C) is committed to the coordination of activities between the ERM/ICP and the Payment Integrity Program to leverage best practices in internal controls.

Human Capital

Currently, the Department has the human capital it needs to reduce improper payments in the Military Retirement program to the levels the Department has targeted. However, as the Military Retirement program evolves and DoD operations change, additional skill sets and personnel resources may be needed to sustain and advance the program.

Information Systems and Other Infrastructure

The Department has the information systems and other infrastructure it needs to reduce improper payments in the Military Retirement program to the levels the Department has targeted. As technology advances, the Department continues to consider improving the accuracy and efficiency of Military Retirement through implementation of new retiree and annuitant pay systems and enhancements to existing systems.

DoD Travel Pay

Internal Controls

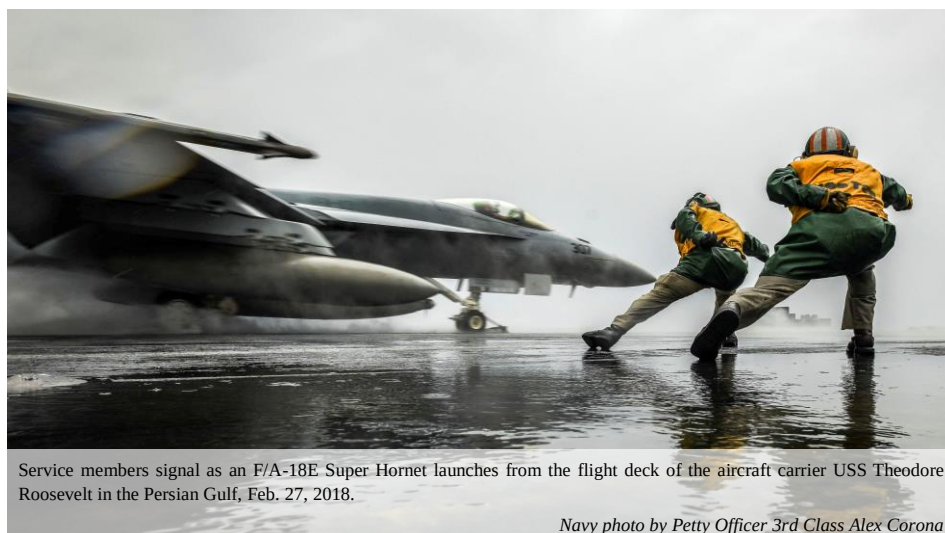
The Department has the internal controls in place to support the reduction of improper payments in the DoD Travel Pay program to the levels the Department has targeted. In addition, OUSD(C) is committed to the coordination of activities between the ERM/ICP and the Payment Integrity Program to leverage best practices in internal controls.

Human Capital

Currently, the Department has the human capital it needs to reduce improper payments in the DoD Travel Pay program to the levels the Department has targeted. However, as the DoD Travel Pay program evolves and DoD operations change, additional skill sets and personnel resources may be needed to sustain and advance the program.

Information Systems and Other Infrastructure

The Department has the information systems and other infrastructure it needs to reduce improper payments in the DoD Travel Pay program to the levels the Department has targeted. The primary system currently used by the Department to process travel payments is DTS. DTS received an unmodified SOC 1 Type 2 report under SSAE No. 18 in FY 2018. However, as technology advances, the Department continues to consider ways to improve the accuracy and efficiency of travel pay through implementation of new travel and entitlement processing systems and enhancements to existing systems.



VII. Sampling and Estimation

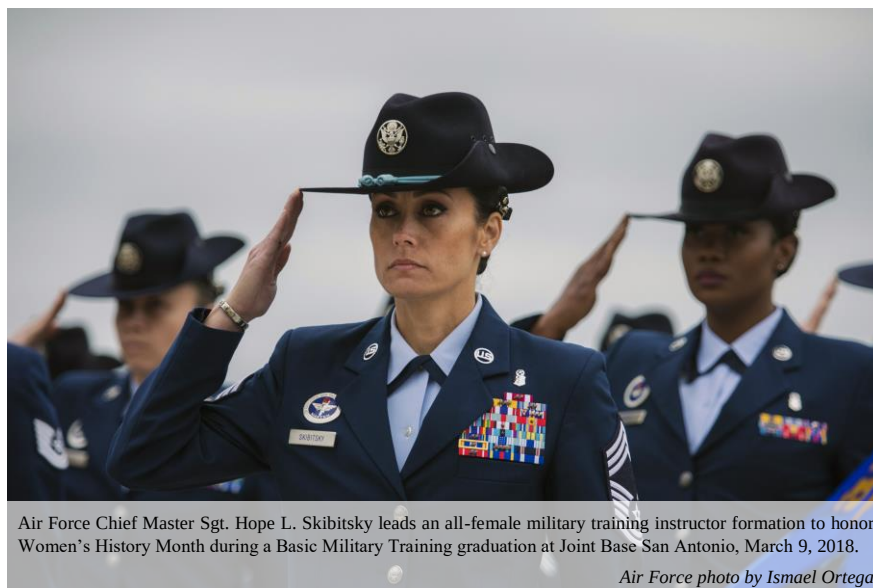
The primary disbursing DoD Components use statistically valid and rigorous methods that are designed to meet or exceed OMB's requirements of a 95% confidence level and a margin of error of +/- 3.0%. By using these methods, disbursing DoD Components are able to identify valid sample sizes and project improper payment percentages for the Department's Payment Integrity Program. The smaller disbursing DoD Components normally perform 100% post-payment reviews or a full review of payments above a specific dollar threshold, with random sampling for lower dollar payments.

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 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% confidence interval and a margin of error of +/- 2.5%. 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 Military Service. DFAS reviewed the sampled pay accounts and calculated estimates of improper payments.

In FY 2019, based on a recommendation made by the Government Accountability Office (GAO) in Report No. [GAO-18-377](#), the Department is revising its post-payment review procedures for this program to include verification of Military Service members pay and allowances with sufficient supporting documentation.



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% confidence interval and a margin of error of +/- 2.5%.

In FY 2018, DFAS updated 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 DTS and 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% confidence interval and a margin of error of +/- 2.5%. 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 DTS stratified by component (i.e., Army, Navy, Marine Corps, Air Force, and other DoD Components) and vouchers from WinIATS stratified by travel type (i.e., Active, Reserve, Casualty, Contingency, Civilian Permanent Change of Station (PCS), other DoD Component, 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 Post-pay 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 RTS estimate, and the Marine Corps' WinIATS estimate.

In FY 2018, DFAS segregated the U.S. Special Operations Command ([USSOCOM](#)) data from the DTS Defense Agencies population and sampled it separately in order to provide USSOCOM with more detailed information regarding the root causes of their travel pay errors. DFAS selected USSOCOM because it accounts for the largest number of travel vouchers amongst the Defense Agencies.

Fraud Reduction Report

The Fraud Reduction and Data Analytics Act of 2015 ([FRDAA](#)) was enacted on June 30, 2016 to help improve federal agencies' financial and administrative controls and procedures to assess and mitigate fraud risks and to improve federal agencies' development and use of data analytics for the purposes of preventing, detecting, and responding to fraud. The FRDAA requires agencies to (1) conduct an evaluation of fraud risks and use a risk-based approach to design and implement financial and administrative control activities to mitigate identified fraud risks; (2) collect and analyze data on detected fraud to monitor fraud trends and use the data and information to continuously improve fraud controls; and (3) use the results of monitoring, evaluation, audits, and investigations to improve fraud prevention, detection, and response.



A Marine ascends out of a cave at Marine Corps Air Station Futenma, Japan, April 19, 2018, during training to detect chemical or radiological threats in difficult-to-access areas.

Marine Corps photo by Cpl. Charles Plouffe

In support of its FRDAA compliance efforts in FY 2018, the Department developed an enterprise-wide Fraud Risk Management framework to assist DoD Components with implementing the requirements of the FRDAA. The framework is a set of guidance and toolkits which will assist DoD Components in achieving the following outcomes:

- Implementing the fraud risk principle in the Government Accountability Office ([GAO](#)) Standards for Internal Control in the Federal Government (“[Green Book](#)”) and the leading practices identified in the July 2015 GAO Report No. [GAO-15-593SP](#), *A Framework for Managing Fraud Risks in Federal Programs*;
- Identifying existing control activities that relate to fraud risk management, opportunities for expanding the scope of those control activities, and fraud risk areas that require the implementation of new control activities; and
- Identifying risks and vulnerabilities to fraud, including with respect to payroll; beneficiary payments; grants; large contracts; information technology and services; purchase, travel, and fleet cards; and commissary.

Further, the Department conducted a pilot program of its framework with select DoD Components to obtain feedback to help enhance the framework's applicability and effectiveness. Feedback received from the pilot program included recommendations to develop a list of frequently asked questions (FAQs), consolidate the framework's toolkits, provide additional potential examples of fraud schemes, highlight the operational benefits of FRDAA compliance, and provide additional fraud risk management training. The Department is working to address each of these recommendations prior to the planned Department-wide implementation of its framework in FY 2019. Once fully implemented, the framework will help raise the maturity level of fraud risk management efforts across the Department and help facilitate the development of an enterprise-wide fraud risk profile. The fraud risk profile, which includes an analysis of the types of internal and external fraud risks, the perceived likelihood and impact of fraud risks, management's risk tolerance, and a prioritized inventory of fraud risks, will assist the Department in the development of an enterprise-wide anti-fraud strategy.

In addition to the steps taken to develop and implement the Fraud Risk Management framework, the Department revised its Enterprise Risk Management and Internal Control Program policies and procedures to align with the updated guidance provided by Office of Management and Budget (OMB) [*Circular No. A-123*](#). This effort included developing an Internal Control Guide to assist DoD Components with strengthening their internal controls and updating the Statement of Assurance Handbook to incorporate FRDAA requirements.

The Department also continued to participate in meetings with the OMB working group tasked by the FRDAA to oversee the scope and development of an inter-agency library to improve the sharing of fraud risk management best practices and data analytics techniques for preventing, detecting, and responding to fraud. As part of this endeavor, the Department contributed to OMB's development of a fraud taxonomy, which is intended to serve as a comprehensive system to effectively communicate fraud risks across the Federal Government, by identifying fraud risks and data analytic approaches for asset misappropriation and procurement fraud. The lessons learned and best practices identified during these activities will be communicated with program managers to further enhance Department-wide fraud prevention and detection.



Reduce the Footprint

Consistent with Section 3 of OMB [Memorandum M-12-12](#), OMB Management Procedures [Memorandum No. 2015-01](#), and the [National Strategy for the Efficient Use of Real Property](#), the Department sets annual targets to reduce the total square footage of domestic office and warehouse inventory compared to the FY 2015 baseline as part of the annual Real Property Efficiency Plan submission to OMB and the General Services Administration. Exhibit 24 and Exhibit 25 present the Department's Reduce the Footprint comparisons of FY 2017 office and warehouse square footage and operations and maintenance costs to the FY 2015 baseline.

Exhibit 24. Reduce the Footprint Baseline Comparison

Square footage (\$ in millions)	FY 2015 Baseline	FY 2017	Change (FY 2017 - FY 2015 Baseline)
	\$ 339.3	\$ 284.6	\$ (54.7)

Through FY 2017, the Department reduced its office and warehouse inventory by over 54 million square feet by focusing on various methods such as consolidation of underutilized assets, termination of leases, and demolition of excess facilities. Additionally, the Department continued conducting physical inspections and inventories of real property in preparation for the FY 2018 full-scope financial statement audit. These tests of existence and completeness led to the discovery of assets which were not previously reported correctly in the Department's accounting records.

Exhibit 25. Reporting of Estimated Operation and Maintenance Costs – Owned and Direct Lease Buildings

Operation and Maintenance Costs (\$ in millions)	FY 2015 Reported Costs	FY 2017	Change (FY 2017 - FY 2015 Baseline)
	\$ 829.5	\$ 895.9	\$ 66.4

Through FY 2017, the Department's estimated annual operation and maintenance costs of its owned and direct leased facilities increased more than \$66 million. The Department's operation and maintenance costs are funded, managed, and disbursed at the base or installation level as opposed to the asset level (e.g., by facility). As a result, the Department is not currently able to trace the actual operations and maintenance costs associated with its office and warehouse inventory at the asset level and must rely on estimates mathematically derived from the allocation of base or installation level costs to all of the various facilities contained therein. As the Department's office and warehouse inventory represents less than 15% of the total DoD real property footprint, changes in the calculated allocation of operations and maintenance costs to office and warehouse space may potentially be driven by factors unrelated to the office and warehouse facilities.

Civil Monetary Penalty Adjustment for Inflation

The Federal Civil Penalties Inflation Adjustment Act Improvements Act of 2015 ([the 2015 Act](#)), which amended the Federal Civil Penalties Inflation Adjustment Act of 1990 ([Inflation Adjustment Act, 28 U.S.C. § 2461, note](#)), requires federal agencies to annually adjust the level of civil monetary penalties for inflation to improve their effectiveness and maintain their deterrent effect. The implementation of this law helps deter violations of law; encourages corrective actions for existing violations; and helps prevent fraud, waste, and abuse within the Department.

The Department publishes its civil monetary penalties adjustments as two separate final rules in the [Federal Register](#) – one containing the adjustments related to the U.S. Army Corps of Engineers ([USACE](#)) and one containing the adjustments related to the remainder of the Department. Exhibit 26 provides the civil monetary penalties that the Department may impose, the authority for imposing the penalty, the year enacted, the year of the latest adjustment, and the current penalty level. Additional supporting details about these penalties are available at Federal Register Volume 83, page 3077 ([83 FR 3077](#)) and [83 FR 19180](#).

Exhibit 26. FY 2018 Civil Monetary Penalty Adjustments for Inflation

Penalty (Name or Description)	Statutory Authority	Year Enacted	Latest Year of Adjustment	Current Penalty (S amount or range)	Sub-Agency / Bureau / Unit	Location for Penalty Updates
Unauthorized Activities Directed at or Possession of Sunken Military Craft	National Defense Authorization Act for FY 2005, 10 U.S.C. § 113, note	2004	2018	\$129,211	Department of the Navy	83 FR 3077 (January 23, 2018)
Unlawful Provision of Health Care	10 U.S.C. § 1094(c)(1)	1985	2018	\$11,346	Defense Health Agency	84 FR 3077 (January 23, 2018)
Wrongful Disclosure - Medical Records	10 U.S.C. § 1102(k)	1986	2018	\$6,709 (First Offense) \$44,726 (Subsequent Offense)	Defense Health Agency	85 FR 3077 (January 23, 2018)
Violation of the Pentagon Reservation Operation and Parking of Motor Vehicles Rules and Regulations	10 U.S.C. § 2674(c)(2)	1990	2018	\$1,848	Deputy Chief Information Officer	86 FR 3077 (January 23, 2018)
Violation Involving False Claim	31 U.S.C. § 3802(a)(1)	1986	2018	\$11,181	Office of the Inspector General	87 FR 3077 (January 23, 2018)
Violation Involving False Statement	31 U.S.C. § 3802(a)(2)	1986	2018	\$11,181	Office of the Inspector General	88 FR 3077 (January 23, 2018)
Class I Civil Administrative Penalties for Violations of Clean Water Act Section 404 Permits	Clean Water Act, 33 U.S.C. § 1319(g)(2)(A)	1987	2018	\$21,394 per violation, with a maximum of \$53,484	U.S. Army Corps of Engineers	83 FR 19180 (May 2, 2018)
Judicially Imposed Civil Penalties for Violations of Clean Water Act Section 404 Permits	Clean Water Act, 33 U.S.C. § 1344(s)(4)	1987	2018	Maximum of \$53,484 per day for each violation	U.S. Army Corps of Engineers	84 FR 19180 (May 2, 2018)
Civil Administrative Penalties for Violations of Section 205(e) of the National Fishing Enhancement Act	National Fishing Enhancement Act, 33 U.S.C. § 2104(e)	1984	2018	Maximum of \$23,426 per violation	U.S. Army Corps of Engineers	85 FR 19180 (May 2, 2018)

Grants Oversight and 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 federal grant awards (including cooperative agreements). To accomplish this, the GONE Act required, among other things, that the head of each federal agency (1) submit a report to Congress in FY 2017 which identifies and quantifies federal grant awards which had been expired for more than two years but had not been closed out and (2) submit a follow-up report to Congress in FY 2018 which discloses progress made in closing out the previously reported expired grant awards. Exhibit 27 provides information related to the expired federal grant awards previously disclosed in the Agency Financial Report for FY 2017 which were not closed out as of September 30, 2018.

Exhibit 27. Unclosed Previously Reported Expired DoD Grant and Cooperative Agreement Awards as of September 30, 2018

Category	2 - 3 Years	> 3 - 5 Years	> 5 Years
Number of Grants / Cooperative Agreements with Zero Dollar Balances	631	554	413
Number of Grants / Cooperative Agreements with Undisbursed Balances	423	147	141
Total Amount of Undisbursed Balances	\$ 37,714,877	\$ 37,456,451	\$ 13,923,750

During FY 2018, the Department successfully closed out 54% of the expired federal grant awards that were previously reported in FY 2017. To achieve this progress in closing out the identified federal grant awards, the Department instituted a number of business process improvements such as

- Increasing staff (both newly hired civilian employees as well as contractors) to reduce the backlog of expired federal grant awards requiring closeout;
- Using new systems that now track closeout requirements, thereby assisting grants offices in tracking when awards are ready to closeout;
- Increasing collaboration between the offices awarding federal grants and those administering the federal grant award; and
- Establishing new business practices to batch federal grant awards by recipient, thereby reducing the burden of the closeout process for both the grant officer and the grantee.

Additionally, through an increased emphasis on data reconciliation during FY 2018, the Department discovered that 415 expired federal grant awards were erroneously reported in FY 2017 and were, in fact, closed.

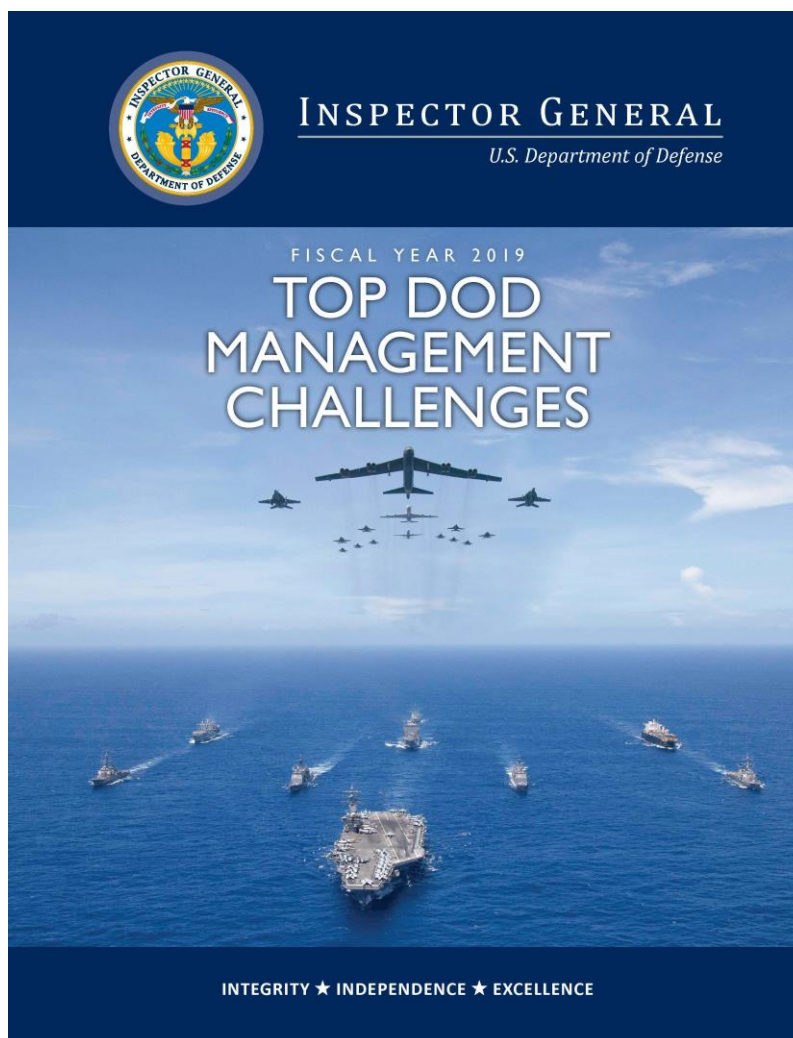
Despite these efforts, many challenges remain such as the lack of adequate staffing, delays caused by DoD and grantee staff changes, and the lack of a centralized system for the management and reporting of federal grant awards. The Department continues to actively research mitigation strategies for these and other challenges, among which include sponsoring Department-wide grant management workshops to facilitate the sharing of best practices, working to develop guidance for the process of closing out federal grant awards, and exploring options for the centralization of federal grant award report collection.

Management Challenges

In accordance with the [Reports Consolidation Act of 2000](#), the DoD Inspector General ([DoD IG](#)) prepares an annual statement that summarizes what the DoD IG considers to be the most serious management and performance challenges facing the Department. This statement is included in a larger report by the DoD IG which provides additional background and descriptive information about each challenge and provides an assessment of the Department's progress in addressing the challenges.

The DoD Office of the Inspector General uses the DoD IG report as a research and planning tool to identify areas of risk in DoD operations. As the report is forward-looking and outlines the most significant management and performance challenges facing the Department now and in the future, it is labelled as FY 2019 rather than FY 2018 to reflect its forward-looking orientation.

The DoD IG's statement summarizing the most serious management and performance challenges facing the Department is included on the following page. The complete DoD IG report on FY 2019 Top DoD Management Challenges as well as reports from previous years are available at the [DoD IG website](#).





**INSPECTOR GENERAL
DEPARTMENT OF DEFENSE**
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October 15, 2018

Each Inspector General (IG) is required by law, the Reports Consolidation Act of 2000, to prepare an annual statement that summarizes what the IG considers to be the “most serious management and performance challenges facing the agency” and to assess the agency’s progress in addressing those challenges. The law states that the “agency head may comment on the IG’s statement, but may not modify the statement.” The law also requires the IG’s statement to be included in the agency’s Financial Report.

The following is the DoD Office of Inspector General’s (OIG) statement on the top management and performance challenges facing the DoD. The DoD OIG identified these challenges based on a variety of factors, including DoD OIG oversight work, research, and judgment; oversight work done by other DoD components; oversight work conducted by the GAO; and input from DoD officials. While we reviewed DoD statements, documents, and assessments of these and other critical issues, we identified these top challenges independently.

The DoD OIG also uses this document to determine areas of risk in DoD operations and where to allocate the DoD OIG oversight resources. This document is forward looking and identifies the top challenges facing the DoD in FY 2019 and in the future.

As reflected in this document, the top 10 DoD management and performance challenges are:

1. Implementing DoD Reform Initiatives
2. Countering China, Russia, Iran, and North Korea
3. Countering Global Terrorism
4. Financial Management: Implementing Timely and Effective Actions to Address Financial Management Weaknesses Identified During the First DoD-Wide Financial Statement Audit
5. Improving Cyber Security and Cyber Capabilities
6. Ensuring Ethical Conduct
7. Enhancing Space-Based Operations, Missile Detection and Response, and Nuclear Deterrence
8. Improving Readiness Throughout the DoD
9. Acquisition and Contract Management: Ensuring that the DoD Gets What It Pays For On Time, at a Fair Price, and With the Right Capabilities
10. Providing Comprehensive and Cost-Effective Health Care

In this document, we discuss each challenge, actions taken by the DoD to address the challenge, and oversight work by the DoD OIG and others related to the challenge.

These challenges are not listed in order of importance or by magnitude of the challenge. All are critically important management challenges facing the DoD.

Glenn A. Fine
Principal Deputy Inspector General
Performing the Duties of Inspector General

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