Defense Health Program

★★★ Agency Financial Report ★★★

Fiscal Year 2019

Introduction

Agency Head Message

It's an exciting time to be part of the Military Health System (MHS)—a time of new and emerging opportunities as we push the military medical enterprise beyond the status quo, and identify new ways of doing business to integrate readiness and health, increase effectiveness, and most efficiently deliver the highest quality services possible to our 9.5 million active duty, retiree, and family member beneficiaries. As we plan for a more integrated, higher-performing enterprise, finding areas to elevate collective MHS performance is critical to delivering on our dual missions of readiness and healthcare delivery.

In Fiscal Year (FY) 2018 and for the first time ever, the MHS' Defense Health Program (DHP) consolidated financial statements were audited by an Independent Public Accounting firm. In our second year under audit, FY 2019, incremental progress has begun for our path to full remediation, but much work remains. The results of the audit found that we need to do better in several areas, most notably: actively managing access to our information technology systems; understanding and explaining adjustments made by the Defense Finance and Accounting Service to our financial statements; consistently accounting for medical services provided to federal trading partners; and ensuring we properly record medical accounts receivable. The audit is and will continue to be an important element in helping the MHS identify deficiencies in our internal business practices. We must now apply the lessons learned from the audit to develop and implement corrective actions, strengthen our internal controls, and reinforce to our beneficiaries and the U.S. taxpayers that we remain vigilant and steadfast in our commitment to maximize resources and deliver world-class healthcare to our warfighters and patients.

During FY 2019, we are continuing our efforts to correct identified issues, improve the accuracy of our financial information, and fortify MHS-wide internal control and accounting practices. We are continuously striving toward the goal of demonstrating that our financial and performance information is complete, reliable, and accurate. I encourage leaders to read this report, share it with your team, and make clear that financial improvement and audit remediation actions are relevant to the entire workforce. Audit is everyone's responsibility.

The MHS spans the globe in support of our service members and their families. We will build a more transparent, efficient, and effective medical enterprise. Our commitment to this effort remains unwavering.

Signed

Thomas P. McCaffery
Assistant Secretary of Defense for Health Affairs

About the Agency Financial Report

The Defense Health Program (DHP) Agency Financial Report (AFR) provides financial and summary performance results enabling the President, Congress, and the American people to assess its accomplishments, and to understand its financial results and operational functions. This AFR satisfies the reporting requirements of the following:

- Federal Managers' Financial Integrity Act of 1982;
- Chief Financial Officers Act of 1990;
- Government Management Reform Act of 1994;
- Reports Consolidation Act of 2000;
- Office of Management and Budget Circular No. A-136, *Financial Reporting Requirements*;
- Improper Payments Elimination and Recovery Improvement Act of 2012;
- Office of Management and Budget Memorandum M-12-12, *Promoting Efficient Spending to Support Agency Operations*; and
- Fraud Reduction and Data Analytics Act of 2015.

The Military Health System (MHS) chooses to produce an AFR rather than the alternative Performance and Accountability Report. The Annual Performance Report, with detailed performance information that meets the requirements of the Government Performance and Results Modernization Act of 2010 (GPRAMA), will be provided within the Annual Performance Plan and Report and transmitted with the release of the Congressional Budget Justification. As of November 15, the DHP AFR may be viewed online at www.health.mil/HealthAffairs. The AFR consists of three primary sections:

Management's Discussion and Analysis

Provides a high-level overview of the MHS, including its history, mission, and organizational structure; the MHS's overall performance related to its strategic goals and primary objectives; management's assurance on internal controls; and forward-looking information.

Financial Section

Contains financial statements, accompanying notes, required supplementary stewardship information, required supplementary information, as well as the independent auditor's report on the financial statements and management's response to that report.

Other Information

Details MHS's compliance with, and commitment to, specific regulations, including performance and management analyses and recommendations from the Office of the Inspector General (IG).

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I. Management's Discussion and Analysis

Mission and Organizational Structure

History

American military medicine traces its origins back to July 27, 1775. For 218 years and until Fiscal Year (FY) 1993, each of the Military Departments funded their respective healthcare operations from within their own appropriations. As advances in medicine and medical technologies emerged, across the nation and within the Department of Defense (DoD), healthcare costs escalated rapidly and began to consume larger portions of the DoD budget. In consequence, in an effort to control the ever-increasing healthcare costs of the DoD, and to lend greater visibility into healthcare expenditures, effective FY 1993 Congress directed the establishment of a unified DoD medical appropriation, namely, the DHP appropriation that would be used to fund the operations of the Military Health System (MHS).

On December 14, 1991, the Deputy Secretary of Defense signed Program Budget Decision 742 to consolidate all medical resources under the control of the Assistant Secretary of Defense for Health Affairs, ASD(HA), and to make other required adjustments to the medical program.

The three Military Departments were directed to (1) parse out what they historically spent on medical care, and (2) transfer those amounts from their respective Operations and Maintenance (O&M), Research, Development, Test, and Evaluation (RDT&E), and Procurement appropriations into the new DHP appropriation that would be used to fund the operations of the MHS. Most, but not all healthcare costs were transferred from the Military Departments into the DHP. Some exceptions to the merger were Military Personnel Appropriations (MPA), resources in support of combat operations, field/numbered medical units, hospital ships, ship-board medical operations; and Military Construction (MILCON) funding for medical facilities. MILCON continues to be reflected in the Service MILCON account, but is administered by the ASD(HA). Combat medical support continues to be funded via Military Department funds/or funds appropriated for that purpose (i.e., Other Contingency Operations appropriation).

What is the Defense Health Program?

The DHP is the nomenclature used to describe a congressionally mandated uniform program of medical and dental care for members and certain former members of the uniformed services, and for their dependents. The term "uniformed services" means the armed forces and the Commissioned Corps of the National Oceanic and Atmospheric Administration (NOAA) and of the Public Health Service. In order to fund the peacetime operation of the MHS, there is established within the DoD an account called the "Defense Health Program" with a Treasury Account Symbol of 0130. All sums appropriated to carry out the functions of the Secretary of Defense with respect to medical and healthcare programs of the Department of Defense are appropriated to that account. The Secretary of Defense may obligate or expend funds from the account for purposes of conducting programs and activities under Title 10 United States Code (U.S.C.), Chapter 55, including contracts entered into under section 1079, 1086, 1092 or 1097 of 10 U.S.C.

The ASD(HA) is the principal advisor to the Secretary of Defense and the Under Secretary of Defense for Personnel and Readiness (USD(P&R)) for all DoD health and force health protection policies, programs. The ASD(HA) serves as resource manager for all DoD health and medical financial and other resources and prepares and submits a DoD Unified Medical Program budget to provide resources for the DoD Military Health System (MHS). Consistent with applicable law, the ASD(HA) accounts for all funding for the DoD MHS, including the DHP appropriations account.

The ASD(HA) ensures DHP Funding Authorization Documents (FADs) are issued to the seven MHS financial statement reporting components thru the DHA. The seven components reporting entities comprising the DHP financial statements are: (1) Army Medical Command (2) Navy Bureau of Medicine and Surgery (3) Air Force Medical Service (4) DHA – Contract Resource Management (5) Uniformed Services University of the Health Sciences (6) Transitional Intermediate Management Organization (tIMO) and (7) DHA Financial Operations Division.

More recently, in 2011, the Deputy Secretary of Defense's Task Force on Reform of the MHS led to the creation of the Defense Health Agency (DHA), a Combat Support Agency (CSA). On September 30, 2013, the DoD issued a directive formally establishing the DHA, and on October 1, 2015, the DHA achieved full operating capability.

In early 2017, in response to the National Defense Authorization Act (NDAA) for FY 2017, the DHA began preparing to assume responsibility for the administration and management of Military Medical Treatment Facilities (MTFs) worldwide. The assumption of these responsibilities began on October 1, 2018 and will be phased in over a 3-year period. The DHA published the FY 2017 Strategic Plan to communicate its mission, vision, goals and objectives to best support its workforce, patients, services, and Combatant Commands (CCMDs).

The FY 2017 NDAA enacted significant reforms to the MHS, including changes to the TRICARE Health Plan and existing internal management structures within the DHA. The centralized administration of the MTFs under the authority, direction and control of the DHA provided the opportunity to improve readiness, standardize and improve the patient experience and lower costs through the elimination of unnecessary redundancies.

The provisions in the FY 2017 NDAA are aimed at (1) ensuring a trained and ready health team to support the Joint Force, (2) delivering an improved experience to MHS beneficiaries, and (3) enabling the MHS to act as one. The goals of the FY 2017 NDAA are to improve healthcare for service members, retirees, and their families, while enhancing medical readiness by:

- Improving and maintaining operational medical force readiness
- Enhancing access to high-quality healthcare
- Improving beneficiaries' health outcomes
- Creating health value
- Modernizing TRICARE support contracts
- Driving efficiencies and eliminating waste
- Demanding performance accountability

"As we navigate change within the MHS, our mission remains clear: providing the best possible health care for our Service members and their families"
– VADM Bono

Mission

The MHS' overarching mission is to support a medically ready force and a ready medical force, supporting a more agile workforce. The MHS aims to enhance the DoD and our nation's security by providing healthcare support for the full range of military operations and sustaining the health of all those entrusted to our care. This includes active duty personnel, military retirees, certain members of the Reserve Component, family members, widows, survivors, ex-spouses, and other eligible members. These MHS beneficiaries receive direct care through MTFs, private sector care through TRICARE's civilian provider networks and other authorized TRICARE providers, and prescription and mail order coverage through the TRICARE Pharmacy Program (TPharm).

How We Accomplish Our Mission

The MHS is a global, comprehensive, integrated system comprised of Army, Navy, and Air Force military, civilian and contracted medical professionals that work cohesively to ensure those in uniform are medically ready to deploy anywhere around the globe on a moment's notice.

With over $50 billion in the unified medical budget (which includes DHP's $34.4 billion, Military Personnel Appropriations and Medicare-Eligible Retiree Health Care Fund (MERHCF)'s $10.2 billion, MILPERS's $8.2 billion and MILCON's $0.4 billion dollars) and serving 9.5 million active duty, retiree, and family member beneficiaries, the MHS employs more than 137,000 personnel in 65 hospitals, 412 clinics, and 414 dental clinics at facilities around the globe, as well as in contingency and combat-theater operations worldwide. MHS is more than just combat medicine – it is a complex system that globally integrates:

- Healthcare delivery
- Public health and medical education
- Private sector partnerships
- Cutting-edge medical research and development

Figure 1: *The DHP MHS by the numbers- 2018*[1]

MILITARY HEALTH SYSTEM BY THE NUMBERS - 2018

TYPE OF CARE	AVERAGE NUMBER PER WEEK	ANNUAL SUMMARY
Inpatient Admissions	**Total: 19,274** Military Facilities: 4,337 Network Facilities: 7,133 TRICARE For Life: 7,804	**Total: 979,700** Military Facilities: 204,400 Network Facilities: 363, 900 TRICARE For Life: 411,400
Outpatient Visits	**Total: 2,033,402** Military Facilities: 793,429 Network Facilities: 657,358 TRICARE For Life: 582,615	**Total: 103,900,000** Military Facilities: 39,000,000 Network Facilities: 33,900,000 TRICARE For Life: 31,000,000
Births	**Total: 2,116** Military Facilities: 789 Network Facilities: 1,327	**Total: 107,100** Military Facilities: 37,500 Network Facilities: 69,600
Prescription Workload	**Total: 2,288,296** Military Facilities: 860,507 Network Facilities: 442,710 Home Delivery: 155,236 TRICARE For Life: 829,843	**Total: 115,700,000** Military Facilities: 44,100,000 Network Facilities: 22,400,000 Home Delivery: 6,900,000 TRICARE For Life: 42,300,000

https://www.health.mil/I-Am-A/Media/Media-Center/Patient-Care-Numbers-for-the-MHS

What is TRICARE

Established in 1995, TRICARE is the worldwide DoD purchased healthcare program. As a major component of the MHS, TRICARE brings together the military hospitals and clinics worldwide (often referred to as "direct care," usually in MTFs) with TRICARE network and non-network civilian healthcare professionals, institutions, pharmacies, and suppliers to provide access to the full array of high-quality healthcare services while maintaining the capability to support military operations.

TRICARE offers beneficiaries a family of health plans, based on the following primary options:

- ***TRICARE Prime***: Is comparable to health maintenance organization (HMO) benefits offered in many areas. Each enrollee chooses or is assigned a primary care manager (PCM), a healthcare professional who is responsible for helping the patient manage his or her care, promoting preventive health services (e.g., routine exams and immunizations), and arranging for specialty provider services as indicated. TRICARE Prime's point-of service (POS) option permits enrollees to obtain care from TRICARE-authorized providers other than the assigned PCM without a referral, but with deductibles and cost shares significantly higher than those under TRICARE Standard.
- ***TRICARE Select***: replaced TRICARE Standard and Extra on January 1, 2018. TRICARE Select is an enrollment-based, self-managed preferred provider network plan.
- ***TRICARE for Life (TFL)***: The TFL was created as wraparound coverage to Medicare-eligible military retirees by Section 712 of the Floyd D. Spence FY 2001 NDAA (P.L. 106-398). TFL functions as a secondary payer to Medicare, paying out-of-pocket costs for medical services covered under Medicare for beneficiaries who are entitled to Medicare Part A and who have Medicare Part B based on age, disability, or end-stage renal disease (ESRD). In most instances, Medicare pays first, then TRICARE pays second.
- ***Other Plans and Programs***: Some MHS beneficiaries may qualify for other benefit options depending on their location, Active/Reserve status, and other factors. Some examples are:

[1] https://www.health.mil/I-Am-A/Media/Media-Center/Patient-Care-Numbers-for-the-MHS

- **Premium-based health plans, including:**
  - TRICARE Young Adult (TYA), available for purchase by qualified dependents up to the age of 26
  - TRICARE Reserve Select (TRS), available for purchase by qualified Select Reserve members
  - TRICARE Retired Reserve (TRR), available for purchase by qualified Retired Reserve members
  - TRICARE Dental Program (TDP) and the TRICARE Retiree Dental Program (TRDP; terminated in 2018)
  - Continued Health Care Benefit Program (CHCBP), which provides a Consolidated Omnibus Budget Reconciliation Act-like continuation benefit.
- **Other major benefit plans, including:**
  - The Transitional Assistance Management Program (TAMP), which provides 180 days of premium-free continued access to the TRICARE benefit after release from Active Duty for certain Active Component members separating from Active Duty and Reserve Component members who have served more than 30 consecutive days in support of a Contingency Operation
  - Dental benefits (military dental treatment facilities and claims management for Active Duty using civilian dental services)
  - Pharmacy benefits in MTFs, via TRICARE retail network pharmacies, and through the TRICARE Pharmacy Home Delivery program (formerly called TRICARE Mail Order Pharmacy)
  - Overseas purchased care and claims processing services
- **Supplemental programs, including:**
  - TRICARE Prime Remote (TPR) in the United States and overseas, DoD-Veterans Affairs (VA) sharing arrangements, and joint services
  - Uniformed Services Family Health Plan (USFHP), which provides the full TRICARE Prime benefit, including pharmacy (under capitated payment) to non-Active Duty MHS enrollees at six statutorily specified locations: Washington, Texas, Maine, Massachusetts, Maryland, and New York
  - Chiropractic care limited to Service members (on Active Duty) at certain MTFs only (no purchased chiropractic care)
  - Clinical and educational services demonstration programs (e.g., chiropractic care, autism services, and the Acute Care Demonstration Pilot)

How TRICARE Is Administered

As the administrative agency for TRICARE, the DHA Contract Resource Management (CRM) directorate manages the execution of policy as issued by the ASD(HA) and the oversight, payment, and management of private sector care administered by contracted claims processors. DHA also monitors the identification, recovery, and reporting of improper payments under the TRICARE program as required by Improper Payments Information Act (IPIA) and as amended by the Improper Payments Elimination and Recovery Act (IPERA) and Improper Payments Elimination and Recovery Improvement Act (IPERIA). DHA also manages the dental program, USFHP and pharmacy programs (retail and mail order), and MERHCF.

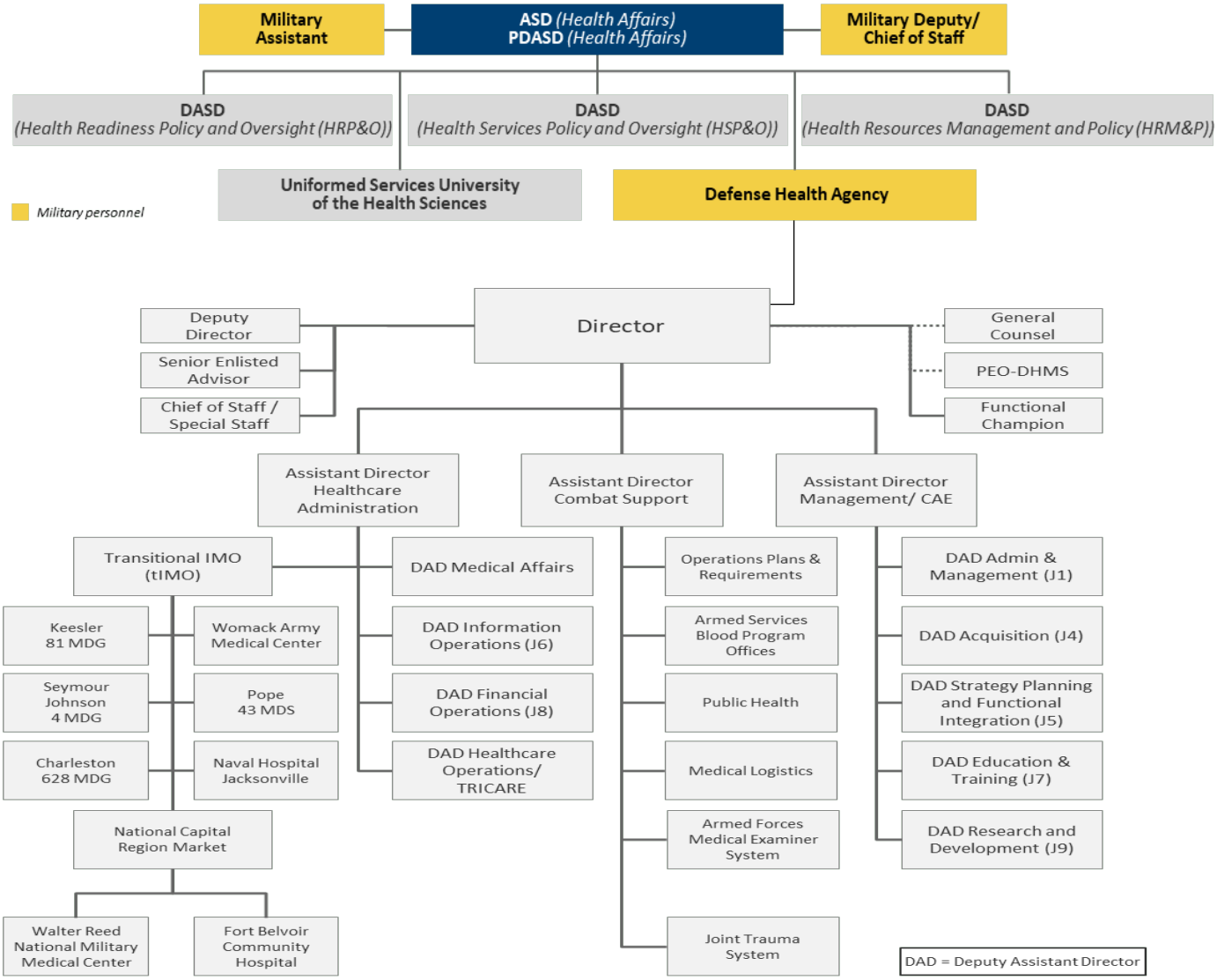
TRICARE is administered on a regional basis, through two regions in the United States (East and West), an overseas contractor aligned with counterpart TRICARE Regional Offices (TROs) responsible for managing purchased care operations and coordinating medical services available through civilian providers with the MTFs, dental, and pharmacy services available through civilian healthcare providers within and outside of the MTFs. The TROs and various other DHA Program Offices do the following:

- Provide oversight of regional operations and health plan administration
- Manage the contracts with regional contractors
- Support MTF Commanders
- Develop business plans for areas not served by MTFs (e.g., remote areas)

The MHS continues to meet the challenge of providing the world's finest combat medicine and aeromedical evacuation, while supporting the TRICARE benefit to DoD beneficiaries at home and abroad. Since its inception more than two decades ago, TRICARE continues to offer an increasingly comprehensive healthcare plan to uniformed services members, retirees, and their families.

Organizational Structure

Figure 2: *MHS organization chart*[2]



[2]SMAs are still direct reports to the Military Departments including Figure 3 and Figure 4.

Figure 3: *Defense Health Program O&M*

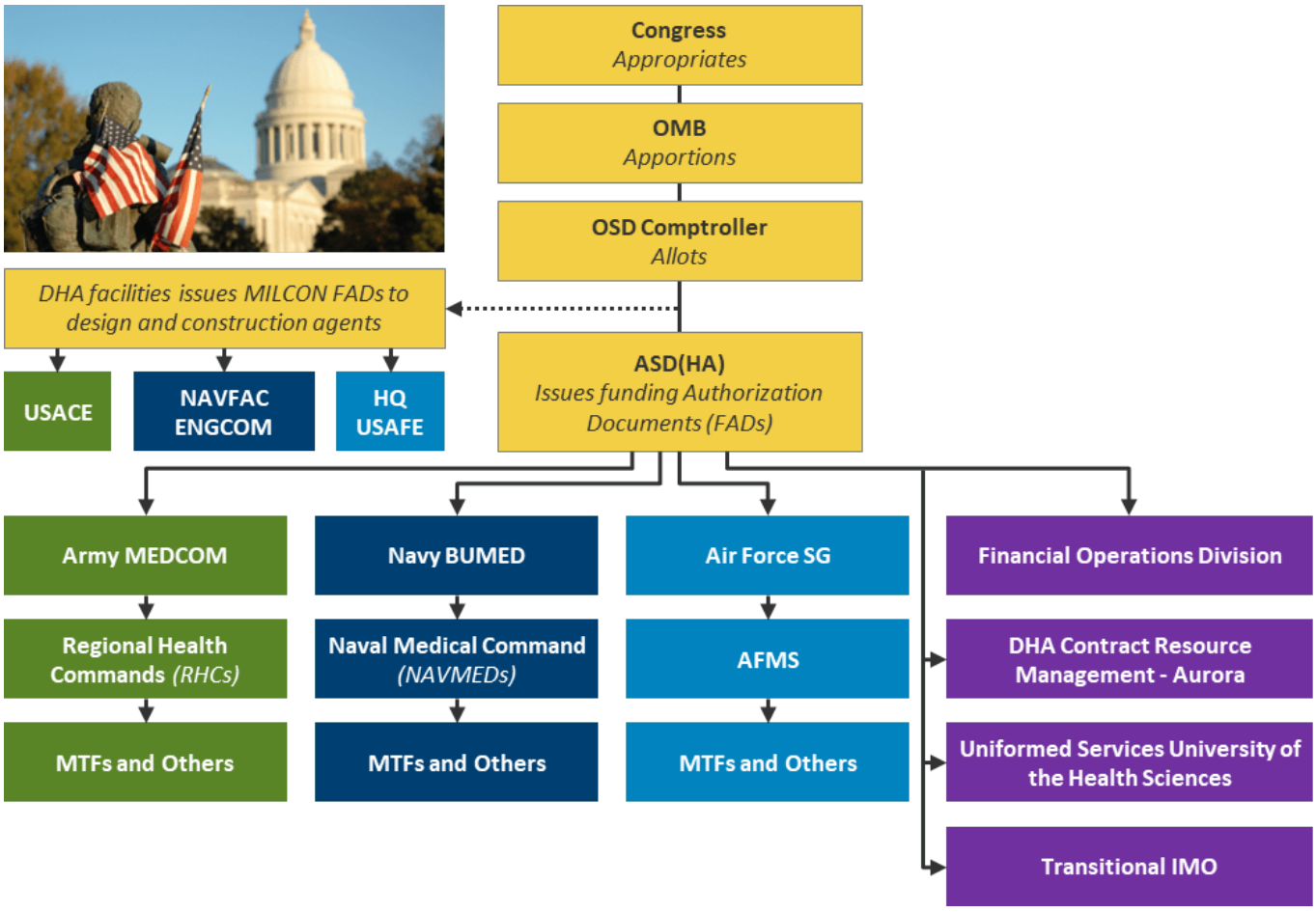
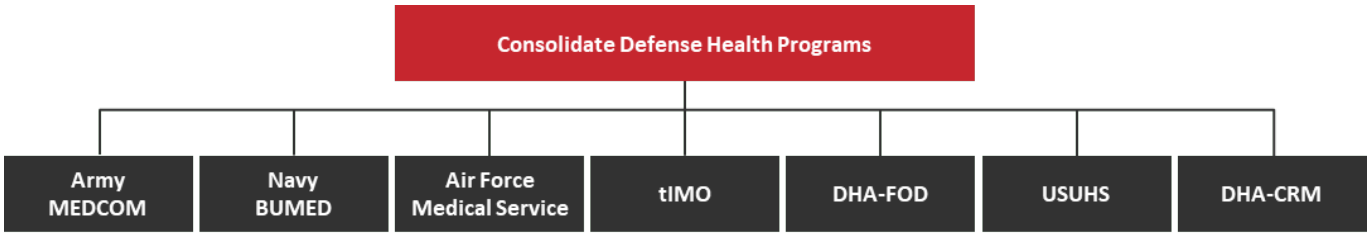


Figure 4: *DHP Defense Department Reporting System (DDRS) Audited Financial Statement (AFS) Compilation Structure*



MHS Components of the DHP Financial Statement Structure

The DHP Financial Statement structure includes the following seven MHS components that receive DHP appropriations:

U.S. Army Medical Command (MEDCOM): MEDCOM provides a premier expeditionary and globally integrated medical force ready to meet the ever-changing challenges of today and tomorrow. As the Army is foundational to the Joint Force, MEDCOM is foundational to the Joint Health Services Enterprise. MEDCOM maintain the diversity and depth to respond to our nation's most demanding expeditionary missions. MEDCOM must ensure the health readiness of the force and maintain responsive medical capabilities to support the Army's three strategic roles: preventing conflict, shaping the strategic security environment, and winning in ground combat. MEDCOM provides sustained health services and research in support of the total force to enable readiness and conserve the fighting strength while caring for soldiers for life and their families.

The Navy Bureau of Medicine and Surgery **(BUMED)**: BUMED delivers medically ready force and ready medical personnel, units, and forces to the Navy and Marine Corps by providing the right capabilities, at the right time, in the right amount, and ready in any environment across the full spectrum of conflict and in peace time. The Surgeon General of the Navy is a principal official on the staff of the Chief of Naval Operations and serves additional duty as Chief, BUMED. He also serves as the chief medical advisor of the Navy and the Marine Corps to the Director of the DHA on matters pertaining to military health readiness requirements and safety of members of the Navy and Marine Corps.

U.S. Air Force Medical Service (AFMS): The AFMS mission is to ensure medically fit forces, provide expeditionary medics, and deliver trusted care to all it serves. The AFMS vision is for its supported population to be the healthiest and highest-performing segment of the U.S. population. Air Force Medics work for the Line of the Air Force. AFMS supports benefit execution and readiness to provide: Healthy/fit force, resilient families, and trained medics. Air Force Warrior Medics...Mission Focused, Excellence Driven.

Defense Health Agency (DHA): The DHA is a joint, integrated CSA that enables MEDCOM, BUMED, and the AFMS to provide a medically ready force and ready medical force to CCMDs in both peacetime and wartime. DHA leads the MHS integrated system of readiness and health to deliver the MHS Quadruple Aim: increased readiness, better health, better care, and lower cost. The DHA oversees the execution of the $34.4 billion DHP appropriation to support the delivery of integrated, affordable, and high-quality health services to the DoD's 9.5 million eligible beneficiaries. The DHA is responsible for driving greater integration of clinical and business processes across the contracted healthcare networks and MTFs. The DHA respects the core values its staff brings while upholding an organizational culture that operates by six guiding principles of transparency, accountability, leading change, empowerment, nurturing, and being team oriented.

Uniformed Services University of the Health Sciences (USUHS): The mission of USUHS is to educate, train, and comprehensively prepare uniformed services health professionals, scientists, and leaders to support the Military and Public Health Systems, the national security and national defense strategies of the United States, and the readiness of our Uniformed Services. On its main campus located in Bethesda, Maryland, and a satellite campus in San Antonio, Texas, USUHS educates and trains outstanding physicians, advanced practice nurses, dentists, allied health professionals, scientists, administrators, and military leaders who are dedicated to career service and leadership in the DoD, United States Public Health Service (PHS), and across the U.S. government. By the end of calendar year (CY) 2021, the vision for USUHS is for it to be widely recognized as the pre-eminent national educational institution for the creation of career uniformed services leaders in the health sciences who are prepared to serve the nation. USUHS will be a focal point for the Uniformed Services in health-related education and training, research and scholarship, leadership development, and support to operational military units around the world. Each USUHS graduate will be a health professional and leader prepared with an outstanding health education, inter-professional health training, leadership training, and a deep and abiding commitment to selfless service, the uniformed services ethos, and the security of the United States.

Transitional Intermediate Management Organization (tIMO): The tIMO is a Joint Tri-Service network of healthcare facilities that provide a medically ready force and ready medical force to CCMDs in both peacetime and wartime. It supports the delivery of integrated, affordable, and high-quality health services and is responsible for driving greater integration of clinical and business processes across the National Capital Region (NCR). The tIMO is a subordinate organization of the DHA and was initially established as a Financial Statement Reporting Entity (FSRE) on October 1, 2013 and designated as the NCR. Effective October 1, 2018, the NCR FSRE was expanded in scope so as to combine the funding activity of Fort Belvoir Community Hospital (FBCH), Walter Reed National Military Medical Center (WRNMMC), Joint Pathology Center (JPC), and various clinics within the Greater Washington D.C. Area, as well as the funding activities of several additional MTFs in the surrounding states and region. The expansion in scope resulted in the NCR being redesignated as the tIMO for the purposes of the DHA organization structure.

Contract Resource Management (CRM) Office: The CRM Office in Aurora, Colorado, is responsible for the accounting, financial support, and financial reporting for TRICARE's centrally funded private sector care programs and the TRICARE Retail Pharmacy Refunds Program. The CRM provides budget formulation input, carries out budget execution, and prepares component financial statements and footnotes. In addition, CRM is responsible for processing invoices received electronically from its contractors and through the TRICE Encounter Data System and reporting these transactions through accessible electronic media. CRM provides funding availability certification and financial program tracking for the centrally funded private sector care programs and monitors budget execution through analysis of current year and prior year's spending and program developments. It also assists DHA's Contract Management, Program Integrity (PI) (fraud), and Case Recoupment division activities related to private sector care.

CRM uses DHP funds provided by annual appropriations to reimburse private sector healthcare providers for services rendered to TRICARE beneficiaries.

Analysis of Performance Goals, Objectives, and Results

Overview

The DHP appropriation funds the MHS under the policy direction and guidance of the ASD(HA). In 2009, the MHS adopted the Quadruple Aim of increased readiness, better health, better care, and lower cost for all components funded by the program. The Quadruple Aim provides direction for each of the MHS components and ensures alignment to the *National Defense Strategy*. The DHA, Service Medical Departments, and USUHS develop strategies to achieve these four aims. The DHA launched the Quadruple Aim Performance Process (QPP) in FY 2019 to begin aligning market and MTF activities with the MHS Quadruple Aim, enhancing an integrated system of readiness and health, and continuous improvement. This process will aid in the transition of the management and administration of MTFs to DHA and demonstrate measurable improvement in DHP's critical initiatives. The Quadruple Aim is defined as:

- **Increased Readiness** means ensuring that the total military force is medically ready to deploy and that the medical force is ready to deliver support health services anytime and anywhere in support of the full range of military operations, including on the battlefield or disaster response and humanitarian aid missions.
- **Better Health** by reducing the generators of disease and injury, encouraging healthy behaviors, increasing health resilience, decreasing the likelihood of illness through focused prevention, and improving the health of those with chronic illness.
- **Better Care** advances healthcare services that are safe, timely, effective, efficient, equitable, and patient- and family-centered. Better care focuses on the health outcomes that matter to patients and their families.
- **Lower Cost** is achieved by focusing on quality, eliminating waste, and reducing unwarranted variation.

Table 1. *DHA's 7 Critical Initiatives*

Quad Aim	Critical Initiatives (CI)	Working Definition of FY 2019 Critical Initiatives
Readiness	Deployability (Medically Ready Force)	Anything that contributes to the **deployability of the active, reserve or guard force**, including care, screening, prevention, or improvements to access for uniformed personnel. This is done in support of Service requirements (readiness demand signal).
	Improve Medical Force Readiness (Ready Medical Force)	All activities that ensure the **medical force is ready to deploy anywhere, anytime** in support of the full range of military operations. It includes efforts to increase readiness related clinical knowledge skills and abilities, but also making sure that the entire team is available for platform specific training, that the facility can support planned and emergent requests for personnel (e.g. Request for Forces (RFFs)), etc. (readiness demand signal).
Better Health	Encourage Healthy Behaviors (Health)	About 50% of health outcomes are related to behaviors. As we shift from healthcare to better health we intend to help patients achieve better health by **making the healthy choice the easy choice**. This is particularly important regarding nutrition, activity, tobacco use, substance abuse, and self-management of chronic illness (health demand signal).
Better Care	Optimize & Standardize Access (Access)	**Patients should not have to wait for help** when they need our help. This initiative is about reducing waiting time for appointments, but it is also about creating alternatives that get help to people without a visit to a hospital or clinic. It is also about reducing time that people have to wait for answers (e.g. lab results) (health demand signal).
	Improve Condition Based Quality Care (Quality)	Our clinic communities are developing pathways of care that will specify the best-known way to deliver care for common conditions like low back pain and normal childbirth. While piloting these efforts, we will implement evidence-based care and **make the right choice the easy choice for the health team** in common conditions (diabetes, low back pain screening, pharyngitis, etc.) (health demand signal).
	Achieve Zero Patient Harm (Safety)	We will **achieve zero harm by identifying zero events** (wrong site surgery, post-operative infections, etc.) **and preventing them with always events** (checklists, care bundles, etc.). This will require changing the culture, lots of training and rigorous process management (health demand signal).
Lower Cost	Improve Effectiveness & Efficiency of DC Platform	Increasing productivity will be accomplished by **eliminating the wasteful processes that prevent our team from performing at full capacity**. We will work smarter, not harder and apply the principles of high reliability to eliminate wasteful procedures, re-work and wasted capacity (efficiency of output).

Strategic performance against each of the four aims is described below. Performance assurance, plans to achieve missed targets, reporting limitations, and the future-state of performance measurement follow.

Improved Readiness

The MHS exists to provide medical and health support to the Uniformed Service Members of the United States for war, combat, humanitarian aid, and disasters. A medically ready fighting force is physically ready to go into combat or support a full range of military operations across the world. A ready medical force has the knowledge, skills, and abilities to provide combat casualty care and other military-relevant health services, anytime and anywhere.

During the Global War on Terror and resulting wars in Afghanistan and Iraq, the MHS made tremendous improvements in combat casualty care. Since 2001, investment in research and clinical care, "produced the lowest case-fatality rate among combat casualties in the history of armed conflict."[3] At the beginning of Operations Enduring Freedom and Iraqi Freedom, the combat-injuring case fatality rate was 18%. That rate steadily decreased to 5% while injury severity increased, helped in part by a Joint Trauma System that accelerated the pace of learning across the MHS. Lessons learned were translated to the civilian community.

In April 2018 the ASD(HA) determined the measures critical to measuring readiness (Table 2). These measures were developed, tested, and implemented in FY 2019.

Table 2: *FY 2019 Military Health System core measures, readiness subset, current as of May 2019 from the Evaluation of the TRICARE Program: FY 2019 Report to Congress*

Quadruple Aim	Measure	Development Status
Improved Readiness	Individual medical readiness	Currently used
Improved Readiness	Percent of providers meeting knowledge, skills, and abilities for general surgery	Currently used for 6 sites
Improved Readiness	Percent of providers meeting knowledge, skills, and abilities for orthopedic surgery	Currently used for 6 sites
Improved Readiness	Active duty Non-Deployability	Currently used
Improved Readiness	Capacity to provide health services for validated request for forces rate ISO conventional force requirements	Under development
Improved Readiness	Capacity to provide health services for validated request for forces rate ISO non-conventional force requirements	Under development
Improved Readiness	Percent of fill against authorized billets	To be developed
Improved Readiness	Defense Readiness Reporting System	Under development

https://www.health.mil/Evaluation of the TRICARE Program FY 2019 Report

[3] "The Laboratory Of War: How Military Trauma Care Advances Are Benefiting Soldiers And Civilians," *Health Affairs Blog*. 2013. DOI: 10.1377/hblog20131218.035947

Better Health

Measuring health outcomes is a newer, less developed field across the healthcare industry. The MHS is exploring the applicability of patient reported outcomes. New evidence illuminates the power of patient reported health outcomes to inform clinical decisions and processes that are more patient-centric than traditional process measures.[4]

The Department fielded the Centers for Disease Control and Prevention's Health-Related Quality of Life measure in the 2016 beneficiary survey. These metric measures self-reported well-being and number of days lost due to illness or injury. The measure data is collected annually and began use in FY 2019. After three years of data collection we will be able to establish a baseline for the military.

Tobacco use, and obesity are leading drivers of early mortality and poor health in the United States, potentially decreasing the medical readiness of the military force. The Department developed health-related measures associated with tobacco use, cessation, and obesity for use in FY 2019. The current status of these measures can be found at Table 3. Targets and thresholds have not yet been developed for these new metrics. The medical community provides tools and programs to help patients achieve an optimal weight and live tobacco-free.

Table 3. *Better health performance in the MHS. For more information about measures, methodology, and performance visit* https://carepoint.health.mil

Measure Name	Current Performance	Data as of	Performance	Longitudinal Time Period
Health Related Quality of Life (HRQOL)	90.2%	9/2018	90.4% to 90.2%, slight decline	9/16 to 9/18
Obesity in Adults	29.8%	12/2018	29.7% to 29.8%, slight improvement	3/16 to 12/18
Obesity in Children	10.2%	12/2018	10.2% to 10.2%, steady performance	3/16 to 12/18
Overweight in Adults	41.5%	12/2018	41.5% to 41.5%, steady performance	3/16 to 12/18
Overweight in Children	14.0%	12/2018	14.0% to 14.0%, steady performance	3/16 to 12/18
Tobacco Counseling	23.3%	12/2018	24.5% to 23.3%, decline in performance	7/16 to 12/18
Tobacco Use Assessment	97.0%	12/2018	97.0% to 97.0%, steady performance	7/16 to 12/18

[4] Weldring T, Smith SMS, "Patient-Reported Outcomes and Patient-Reported Outcome Measures," *Health Serv Insights*. 2013; 6:61-68. DOI: 10.4137/HSI.S11093

Better Care

Patient-centric improvements were made to healthcare delivered by TRICARE programs. There were specific improvements in access, evidenced-based quality of care, and preventable harm events. The measures and longitudinal performance are presented in Table 4, below.

Table 4: *Quality of healthcare services performance in the MHS.*

Measure Name	Current Performance	Refresh Date	Performance	Longitudinal Time Period
Risk adjusted mortality	1.02 standard mortality ratio	9/2018	0.99 to 1.02; slight decline	9/16 to 9/18
Recommend hospital	77.36% recommend	9/2018	75.43% to 77.36%; positive improvement	6/16 to 6/18
Provider communication	83.56% satisfaction w/ outpatient provider	6/2018	76.43% to 83.56%; positive improvement	6/14 to 6/18
Catheter-Associated UTI – SIR	0.419 standard infection ratio	12/2018	1.076 to 0.419; positive improvement	3/13 to 12/18
Central Line-Associated Bloodstream Infection	1.398 infection rate ratio	12/2018	.783 to 1.398; decline	3/13 to 12/18
Wrong Site Surgery	10 wrong site, person, or procedure	3/2019	7 to 10; declining performance	12/12 to 3/19
Unintended Retained Foreign Object (URFO)	2 surgical objects retained	3/2019	3 to 2; positive improvement	12/12 to 12/18
NSQIP All Cases Morbidity	6 cases	6/2017	6 to 6; no change	12/13 to 6/17
NSQIP All Cases Mortality	5 cases	6/2017	4 to 5; slight decline in performance	12/13 to 6/17
Diabetes A1c Testing	91.99% 18-75 with diabetes tested	1/2019	89.71% to 91.99%; positive improvement	1/13 to 1/19
Low back pain	83.03% with low back pain not imaged	1/2019	75.13% to 83.03%; positive improvement	1/16 to 1/19
Children with pharyngitis appropriate testing	93.08% 3-18 year olds tested and prescribed an antibiotic	1/2019	82.55% to 93.08%; positive improvement	1/16 to 1/19
Breast cancer screening	76.03% 52-74 year old women with screening in past 27 months	1/2019	73.91% to 76.03%; positive improvement	1/13 to 1/19
Cervical cancer screening	81.19% 24-64 year old women with screening in past 3 years	1/2019	83.17% to 81.19%; declining performance	1/13 to 1/19
Colon cancer screening	76.41% 51-75 year old screened past 2 years	1/2019	72.78% to 76.41%; positive improvement	1/13 to 1/19
7-day mental health follow-up	73.76% seen within 7 days post-discharge	1/2019	64.25% to 77.66%; positive improvement	1/13 to 12/18
All cause readmissions	0.87 out of 1.00; benchmarked to HEDIS	10/2018	0.92 to 0.87; positive improvement	6/14 to 10/18
Well child	88.17% at 15 months with 6+ well child visits	1/2019	77.03% to 88.17%; positive improvement	1/13 to 1/19
IQI #33 primary caesarean section	13.93% first time delivery without hysterectomy	6/2018	16.05% to 13.09%; positive improvement	3/16 to 6/18
Postpartum hemorrhage	4.14% women who delivered, diagnosed with hemorrhage	6/2018	2.43% to 4.14%; declining performance	3/16 to 6/18
Unexpected newborn complication	4.63% of babies without preexisting conditions with complications	6/2018	5.34% to 4.63%; positive improvement	3/16 to 6/18
Days to 3rd Next 24-hour Appointment	.96 days to 3rd next available same day appointment	4/2019	1.16 to .96; positive improvement	10/15 to 4/19

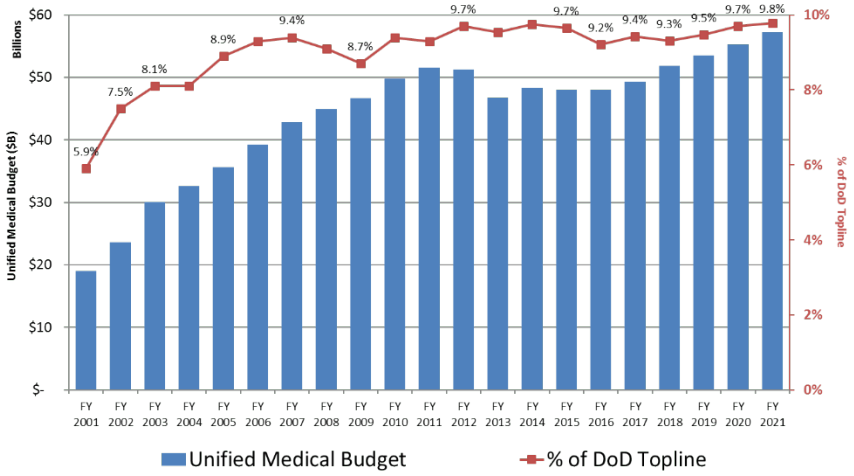
Days to 3rd Next Future Appointment		5.76 days to 3rd next available future appointment	4/2019	5.79 to 5.76; slight improvement	10/15 to 4/19
Primary Care Leakage		10.6% of potentially recapturable PC leakage to the network	1/2019	5.87% to 10.6%; declining performance	10/14 to 1/19
PCM Continuity		58.12% of enrollees seen by their assigned PCM	4/2019	59.89% to 58.12; slight decline in performance	10/15 to 4/19
Access – Secure Messaging		54.36% of Direct Care Enrollees w/Secure Messaging	4/2019	36.2% to 54.36%; positive improvement	5/15 to 4/19
Access – Secure Messaging Response Time		84.54% of patient messages were responded to within 1 day	4/2019	76.85 to 84.54; positive improvement	5/16 to 4/19
Satisfaction with Access to Care		80.65% of patients were satisfied with access to care	9/2018	81.43% to 80.65%; slight decline in performance	12/16 to 9/18
Specialty Care: Referral Order to Book		3.98 days from referral in CHCS to specialty appointment booking	2/2019	4.22 to 3.98; positive improvement	1/16 to 2/19
Specialty Care: Booked to Actual Appointment		15.56 days from date booked to specialty appointment date	2/2019	13.52 to 15.56; declining performance	1/16 to 2/19
Ambulatory Specialty Care Leakage		12.8% of specialty care encounters leaking into the network	2/2019	13.9% to 12.8%; positive improvement	10/13 to 2/19
Active Duty Days to Primary Care Appointment		.52 days from request to appointment for AD	4/2019	.54 to .52; slight improvement	10/17 to 4/19
Active Duty Days to Specialty Care Appointments		13.46 days from referral to appointment for AD Specialty Care	4/2019	13.49 to 13.46; slight improvement	10/17 to 4/19

Red denotes significantly below target, yellow/amber below target, green on target, and blue exceeding target. For more information about measures, methodology, and performance visit https://carepoint.health.mil

Lower Cost

The U.S. Department of Health and Human Services reports that healthcare expenditures rose from 5.0% of Gross Domestic Products (GDP) in 1960 to 17.9% of GDP in 2017.[5] The rise in health care costs to the DoD is commensurate with the civilian employers in the US. The Unified Medical Budget as a total expenditure of the total Defense budget is 9.5% for FY 2019 (Figure 5). The MHS managed to slow the accelerating rate of health costs with greater centralization of processes and decision-making, including more robust enterprise-supporting shared services. Health care cost containment is a priority for the DoD. However, MHS activities are inextricably linked to the civilian health care market.

Figure 5: *Military medical costs as a percentage of the DoD budget.*



***In FY** 2019, the Unified Medical Budget topped US $50 billion. These costs include healthcare for active duty service members, reservists, activated guard, family members, military retirees, and other secretarial designees.*

The MHS tracks monthly per member per month (PMPM) costs. The goal rate is a 2.0% increase per year, a target benchmarked against the Henry J. Kaiser Family Foundation's optimal rate of healthcare cost increase year over year in the US. PMPM rate increase for beneficiaries was .8% in 2018. Total cost per member per month is $328.72 as of September 2018. This represents a 5% decrease in the PMPM cost from 2017.

Pharmaceutical costs drive a considerable portion of healthcare spending in the US. Again, the DoD is not an exception. The Department measures pharmaceutical costs from inpatient facilities, retail pharmacies, and mail-order pharmacies. Retail pharmacies are the costliest and DoD has a goal to keep the percent of pharmacy dollars spent in retail pharmacies under 30% by encouraging MTFs to channel pharmacy workload to the MTFs or mail order pharmacy. In the rolling 12-month average ending in March 2019, 24.7% of pharmacy dollars were spent in retail pharmacies, exceeding performance targets. The Quadruple Aim Lower Cost metrics tracked in the MHS are displayed below in Table 5.

[5] Historical National Health Expenditure Accounts (NHEA) official estimates, cms.gov. US Department of Health and Human Services/Centers for Medicare and Medicaid. 2018.

Table 5. *Lower Cost – Improve Stewardship performance in the MHS.*

Measure Name	Current Performance	Refresh Date	Performance	Longitudinal Time Period
PMPM	.80% PMPM growth rate for Prime Enrollees	9/2018	$333.18 to $328.72; positive improvement	10/13 to 9/18
Total Purchased Care Cost	$731M spent on purchased care	2/2019	$701M to $731M; declining performance	10/13 to 2/19
Private Sector Care Cost Per Prime Enrollee	4.37% YTD Change in Private Sector Care Costs per Prime Enrollee	9/2018	$165.89 to $153.25; positive improvement	10/13 to 9/18
Total Empanelment	.8% increase in total empanelment (rolling 12 mo avg)	4/2019	5.2M to 4.7M	9/12 to4/19
Pharmacy Percent Retail Spend	24.7% of pharmacy dollars spent in retail pharmacies	3/2019	47.6% to 24.7%; positive improvement	10/11 to 3/19
Active Duty Specialty Care Provider Efficiency	28% of AD providers met MGMA benchmark. Proxy for clinical currency.	12/2018	23% to 28%; positive improvement	12/13 to 12/18
Overall Occupancy Rate (US)	58% of inpatient beds occupied	1/2019	61% to 58%; declining performance	10/16 to 1/19
ICU Occupancy Rate (US)	60% of ICU beds occupied	1/2019	61% to 60%; steady performance	10/16 to 1/19

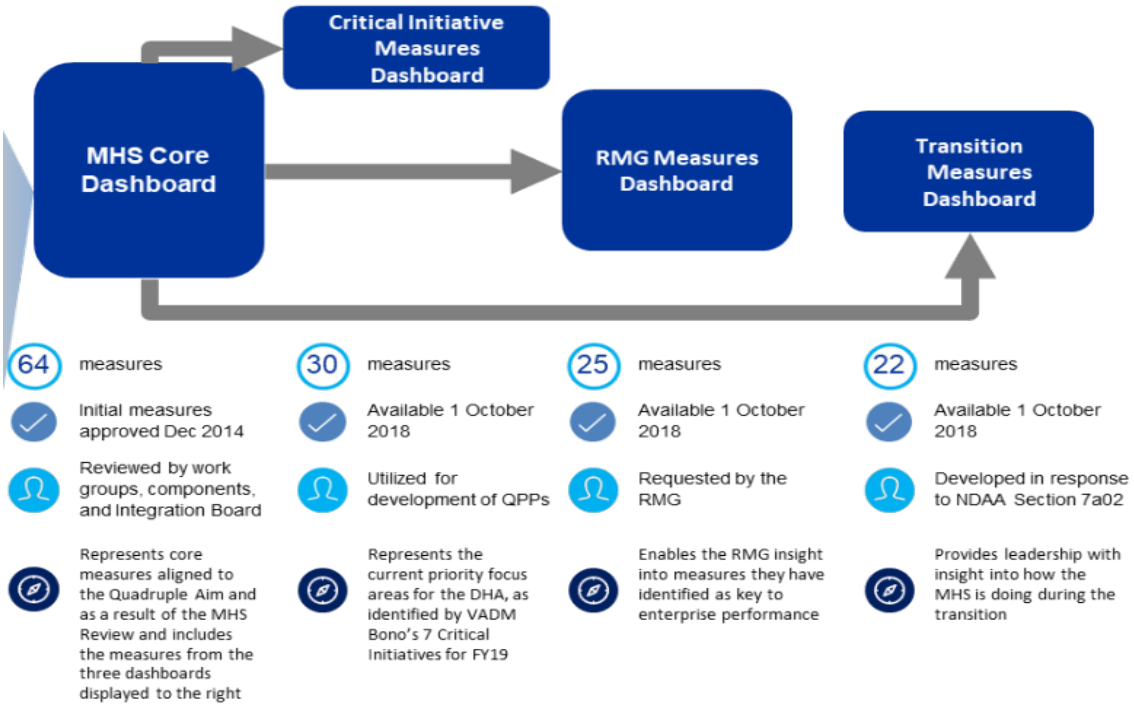
Red denotes significantly below target, yellow/amber below target, green on target, and blue exceeding target. For more information about measures, methodology, and performance visit https://carepoint.health.mil

Performance Information Assurance

The MHS performance data is stored and retrieved in a standardized, controlled process from the MHS Data Repository. The repository, in turn, is accessed through the MHS Mart (M2). These systems are automated with data pushed directly from the legacy electronic health records such as Composite Health Care System (CHCS) and Armed Forces Health Longitudinal Technology Application (AHLTA). MHS GENESIS, the new commercial off the shelf Cerner electronic health record, will integrate with the repository or another platform with similar functionality.

Strategic data, trends, and information are populated on an interactive, web-based platform called CarePoint, accessible at https://carepoint.health.mil. Data is available to all with a DoD Common Access Card. The data cannot be altered by those viewing the dashboards. Analysts in the field also pull data from the M2, although it is for specific data calls at the request of their commands. M2 training is centralized by the DHA, ensuring a common lexicon and data dictionary across the MHS. Four measure sets present current strategic performance: 1) MHS Core Measures; 2) Critical Initiatives Measures utilized for the Quadruple Aim Performance Process; 3) Reform Management Group (RMG) Measures; and 4) NDAA for FY 2017, Section 702-related Transition Measures. All measures are represented in the FY 2019 MHS Core Measures. Breakout of the measures are depicted in Figure 6 below.

Figure 6: *MHS Measures Categories - https://www.health.mil/Evaluation of the TRICARE Program FY 2019 Report*



The ASD(HA) hosts a MHS Review and Analysis meeting on a recurring basis, analyzing performance trends across the enterprise with representation from the Army, Navy, Air Force, DHA, Joint Staff, and USUHS. A full evaluation of the program is delivered to Congress annually.

Plans to Achieve Missed Targets

In FY 2019, the DHA implemented the first round of the QPP. It is the process by which "we" engage the entire MHS to achieve breakthrough performance in pursuit of the Quadruple Aim and establish local, market and enterprise initiatives to close performance gaps. The purpose of the QPP is to:

- Align Market and MTF activities with the MHS Quadruple Aim vision,
- Enhance our integrated system of readiness and health,
- Promote system learning and continuous improvement,
- Support a smooth transition of administration and management of MTFs to DHA and,
- Enable enhanced enterprise performance, balanced across the Quadruple Aim framework – Improved Readiness, Better Health, Better Care, and Lower Cost

The QPP begins with issuing guidance from DHA headquarters to the Markets and MTFs. Upon receipt of QPP guidance MTF / Market Leaders conduct an Executive Planning Session (EPS) to identify both the readiness and health services delivery demand signals in their area of responsibility. These demand signals serve as inputs into a three-year planning process. MTF / Market leaders then evaluate their available supply to respond to their demand signals. Supply, or resources, include both direct care assets as well as those that can be leveraged from our network and private sector partnerships. Understanding both demand and supply, MTFs / Markets are positioned to evaluate current performance against MHS Core Dashboard measures and to develop plans to close gaps in performance, as well as gaps in available supply to meet the demand signal. MTF leaders will signal to their Market if demand exceeds the MTF's capabilities. Likewise, Market leaders will signal to the DHA when they require DHA assistance to close any gaps. Inputs, evaluation and outputs of the QPP are displayed in Figure 7 and the QPP cycle is depicted in Figure 8.

Figure 7: *Inputs, Evaluation, and Outputs of the QPP https://carepoint.health.mil/sites/QPP/SitePages/Home.aspx*

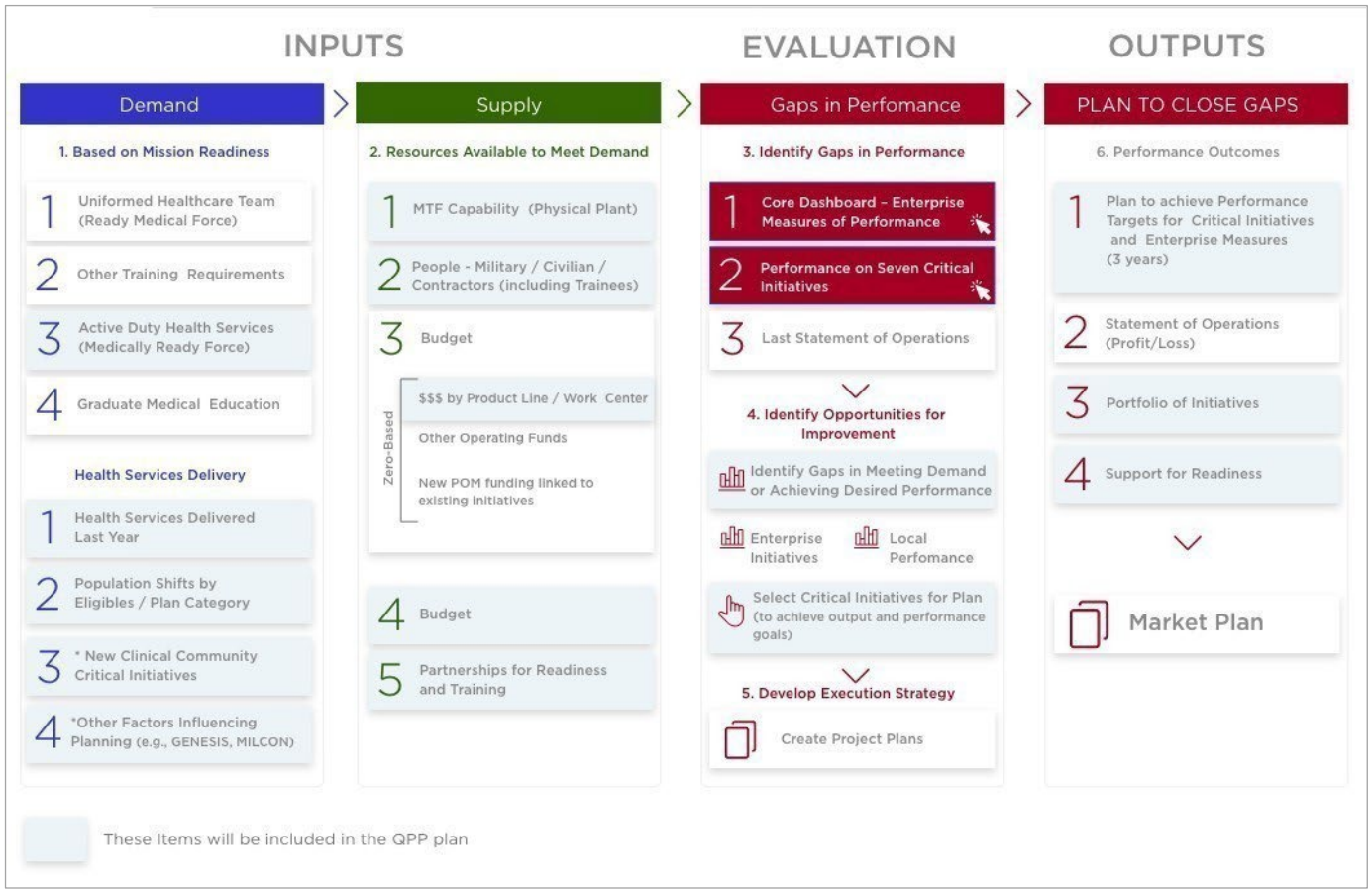
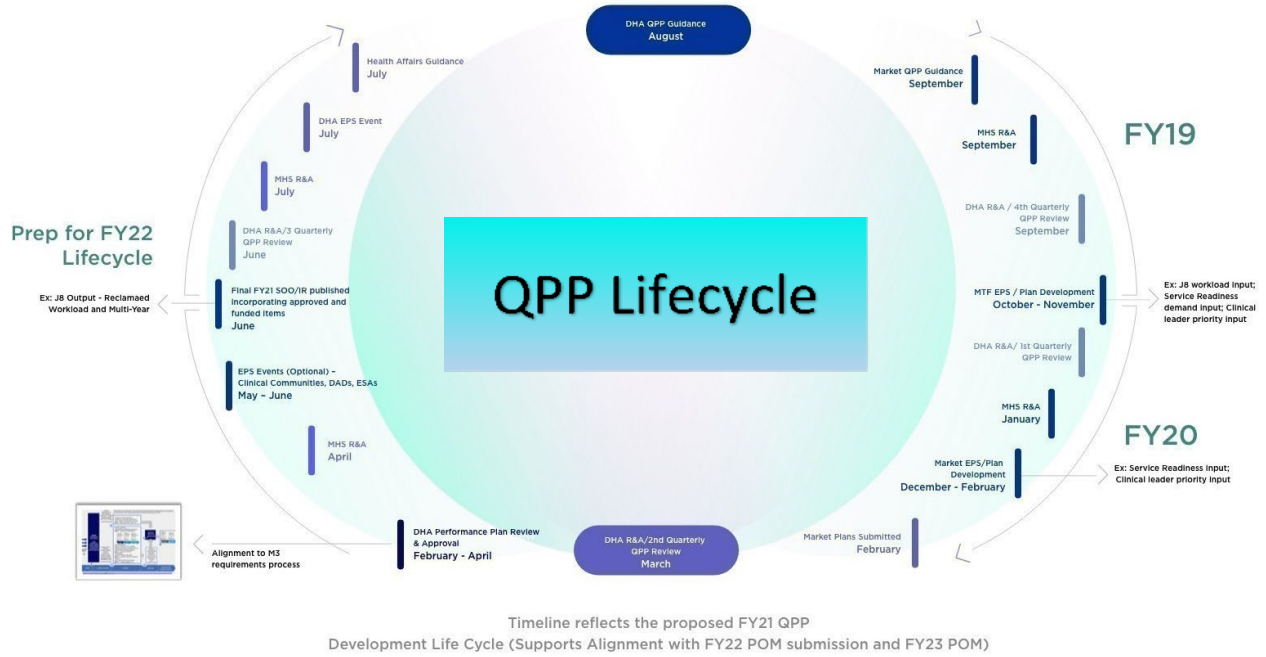


Figure 8: *QPP lifecycle https://carepoint.health.mil/sites/QPP/SitePages/Home.aspx*



Timeline reflects the proposed FY21 QPP
Development Life Cycle (Supports Alignment with FY22 POM submission and FY23 POM)

QPP Plans are evaluated at each level to identify systemic issues, consolidate resources, reduce variation and prioritize work. The results are analyzed, working the Program Objective Memorandum (POM) process, and considered during re-evaluation of enterprise strategy.

Performance Measurement Limitations

MHS is striving to continue standardization of measures across the three military services. Challenges include different measure definitions, difficulty reaching consensus on single measures, and data quality, and timeliness. Healthcare measures in general are often lagging, sometimes outside of the current fiscal year, due to limitations in survey data gathering. Measures from the TRICARE network is limited by availability of data other than claims-based administrative data.

Future Performance Management and Accountability

The NDAA for FY 2017 directs the DoD to streamline the TRICARE health plan for Active Duty, Reservists, and military retirees; transfers authority related to the management and administration of MTFs to the DHA; and to determine an optimal footprint. This transition is expected to reduce the management headquarters burden across the system.

For FY 2020, the MHS core dashboard is composed of sixty-four strategic measures. Measures remain aligned to the Quadruple Aim. The organization will continue to utilize the QPP throughout the transition of MTFs to DHA management and administration. The Quadruple Aim will not change. The four aims are broad and will stand the test of time; there will always be opportunities to improve readiness, health, care, and cost. The same is true of any health system anywhere in the world, albeit without the added challenge of medical readiness.

Analysis of Financial Statements and Stewardship Information

The financial statements of the DHP reflect and evaluate the execution of its mission to provide a medically ready force and a ready medical force to CCMDs in both peacetime and wartime. This analysis summarizes the DHP's financial position and results of operations and addresses the relevance of major types and/or amounts of assets, liabilities, costs, revenues, obligations, and outlays.

The principal statements include a consolidated balance sheet, a consolidated statement of net cost (SNC), a consolidated statement of changes in net position (SCNP), and a combined statement of budgetary resources (SBR). These principal statements are included in the "Financial Section" of this report. The DHP also prepares a combining schedule of budgetary resources within required supplementary information.

Overview of Financial Position

Table 6: *Summary of DHP's major financial activities in as of September 30, 2019 and 2018.*

DHP Major Financial Activities *(dollars in thousands)*				
Net Financial Condition	**FY 2019**	**FY 2018**	**$ Increase/(Decrease)**	**% Increase/(Decrease)**
Fund Balance with Treasury	$ 19,580,243	$ 20,533,206	$ (952,963)	(4.6%)
Accounts Receivable, Net	943,453	1,165,538	(222,085)	(19.1%)
Inventory and Other Assets	85,385	64,003	21,382	33.4%
Property, Plant, and Equipment, Net	3,224,053	3,725,741	(501,688)	(13.5%)
Total Assets	**$ 23,833,134**	**$ 25,488,488**	**$ (1,655,354)**	**(6.5%)**
Accounts Payable	$ 1,116,293	$ 1,001,187	$ 115,106	11.5%
Military Retirement and Other Federal Employment Benefits	256,703,184	251,338,190	5,364,994	2.1%
Accrued Unfunded Annual Leave	321,277	335,237	(13,960)	(4.1%)
Accrued Funded Payroll and Benefits	226,146	215,602	10,544	4.9%
Environmental, Disposal & Other Liabilities	203,053	148,617	54,436	36.6%
Total Liabilities	**$ 258,569,953**	**$ 253,038,833**	**$ 5,531,120**	**2.2%**
Unexpended Appropriations	$ 18,603,336	$ 19,243,749	$ (640,413)	(3.3%)
Cumulative Results of Operations	(253,340,155)	(246,794,094)	(6,546,061)	(2.6%)
Total Net Position	**$ (234,736,819)**	**$ (227,550,345)**	**$ (7,186,474)**	**(3.2%)**
Net Program Cost	**$ 40,083,175**	**$ 29,242,709**	**$ 10,840,466**	**37.1%**
Net Cost of Operations	**$ 40,083,175**	**$ 29,242,709**	**$ 10,840,466**	**37.1%**
Budgetary Resources	**$ 44,359,105**	**$ 44,101,975**	**$ 257,130**	**0.6%**

Preparing the DHP financial statements is a vital component of sound financial management and provides information that is useful for assessing performance, allocating resources, and targeting areas for future programmatic emphasis. The DHP's management is responsible for the integrity of the financial information presented in its financial statements. The DHP is committed to financial management excellence and maintains a rigorous system of internal controls to safeguard its widely dispersed assets against loss from unauthorized acquisition, use, or disposition.

A summary of the DHP's major financial activities as of September 30, 2019 is presented in table 6 above. This table represents the resources available, assets on hand to pay liabilities, and the corresponding net position. The net cost of operations is the cost of operating the programs of the DHP's, less earned revenue. Budgetary resources are funds available to the DHP to incur obligations and fund operations.

Balance Sheets Summary

Assets – What We Own and Manage

Total assets were $23.8 billion as of September 30, 2019. The most significant assets are the fund balance with treasury (FBwT) and Property, Plant, and Equipment, net, which represent 96 percent of the total of DHP's assets. The largest, FBwT, consists of cash appropriated to DHP by Congress or transferred from other federal agencies and held in the U.S. Department of Treasury's accounts that are accessible by DHP to pay the obligations it incurs. Additionally, the increase in Inventory and Other Assets of $21.4 million, or 33 percent, is primarily due to the reversal of $32.5 million of unsupported stockpile materials off of the books of the DHA's Financial Operations Directorate, while successfully valuing $52.0 million of stockpile materials at the BUMED in the form of emergency supplies to be used in the event of a nationwide pandemic. General Property, Plant, and Equipment also decreased by $501.7 million, or 13.5 percent, primarily due to a $392.7 million decrease in the amount of software capitalized on DHP's books and a $196.3 million increase in the amount of DHP's general equipment assets.

Liabilities – What We Owe

Total liabilities of $258.6 billion as of September 30, 2019, of which $256.7 billion, or 99 percent, comprises military retirement and other federal employment benefits. These liabilities represent funds calculated by the DoD's Office of the Actuary (OACT) at the end of each fiscal year using the current active and retired military population plus assumptions (inflation, discount rate, and medical trend) about future demographic and economic conditions. $38.5 million of the $115.1 million increase in the accounts payable in FY 2019 can be explained by an increase in Non-Federal payables due to an increase in the number of TRICARE beneficiaries opting to fill prescriptions through retail pharmacies instead of mail-orders as a result of an increase in co-pays. An additional $39.2 million increase in the accounts payable balance can also be explained by an accrual made by the Uniformed University of the Health that was not booked in FY 2018 and was booked in FY 2019. Finally, $2.5 million of the increase in Environmental, Disposal, and Other Liabilities balance is a result of the annual review and revision of this estimate.

Net Position – What We Have Done Over Time

Net position represents the DHP's net results of activity over the years and includes unexpended appropriations and cumulative net earnings. The DHP's net position is shown on the *Consolidated Balance Sheets* and the *Consolidated Statements of Changes in Net Position*. The reported net position balance as of September 30, 2019, was ($234.7) billion.

Results of Program Cost

Net Costs – What Cost We Incurred for the Year

The net results of operations are reported in the *Consolidated Statements of Net Cost* and the *Consolidated Statements of Changes in Net Position. The Consolidated Statements of Net Cost* represents the cost of operating (net of earned revenues) the DHP's programs. In FY 2019, the DHP operated the following four programs:

- ***Operations, Readiness, and Support****:* Support the total military force by ensuring the medical force is medically ready and prepared to deliver healthcare anytime, anywhere in support of the full range of military operations, including humanitarian missions.

- ***Procurement:*** The DHP appropriation procurement program funds acquisition of capital equipment in MTFs and other selected healthcare activities.
- ***Research, Development, Test, and Evaluation (RDT&E):*** Aid medical force through effective and accountable investments in education and research to establish sustainable improvements in the well-being and productivity of the MHS.
- ***Family Housing & Military Construction:*** Assist military forces based on need according to principles of universality, impartiality, and human dignity to save lives, alleviate suffering, and minimize the economic costs of conflict, disasters, and displacement.

Figure 9: *Summarizes total net program cost by the DHP's programs as of September 30, 2019.*

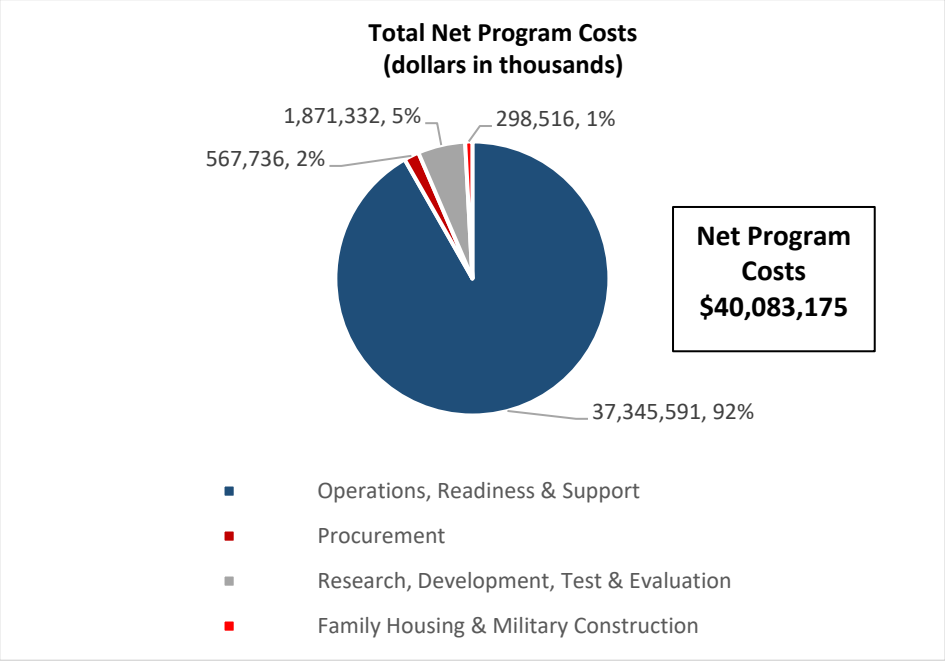


Figure 9 to the left shows the total net program cost of operations of $40.1 billion to operate each of these DHP's program. These costs do not include the gain from actuarial assumption changes. This is approximately a $10.8 billion increase over FY 2018 in net costs, an increase that is due in large part to the $7.7 billion increase in healthcare expenses incurred by the DHA's Contract Resource Management (CRM) component which include changes in the incurred but not reported (IBNR) and actuarial liability expenses. Additionally, the FY 2018 prior year credit balance of ($243.8) million, shown as gross costs related to Family Housing and Military Construction, due to an abnormally large increase in the DHP's cost capitalization offset account caused by adjustments resulting from a process change in the way DHP accounts for Construction in Progress.

Net Costs – Stewardship Investments

The DHP net cost includes outlays and expenses incurred that are expected to benefit the Nation over time. These expenses are qualitatively material and worthy of highlighting as they represent expenses charged to current operations. Summary information regarding these expenses is provided in the table below. An in-depth discussion is provided in the Required Supplementary Stewardship Information section of this report.

Table 7: *Summary of DHP's Stewardship Investment Activities.*

DHP Stewardship Investments Summary *(dollars in thousands)*				
Investment Type	**FY 2019**	**FY 2018**	**$ Increase/(Decrease)**	**% Increase/Decrease**
Research and Development	$ 1,737,572	$ 511,216	$ 1,226,356	239.9%

Budgetary Resources

Our Funds

The *Combined Statements of Budgetary Resources* provides information on the budgetary resources that were made available to DHP during the fiscal year and the status of those resources at the end of the fiscal year. The DHP receives most of its funding from general government funds administered by Treasury and appropriated by Congress for use by DHP. Budgetary resources consist of the resources available to the DHP at the beginning of the year, plus the appropriations received, spending authority from offsetting collections, and other budgetary resources received during the year, such as receipts from the MERHCF Accrual Fund.

Figure 10: *Summarizes obligations incurred, unobligated balances, and total budgetary resources for the DHP as of September 30, 2019.*

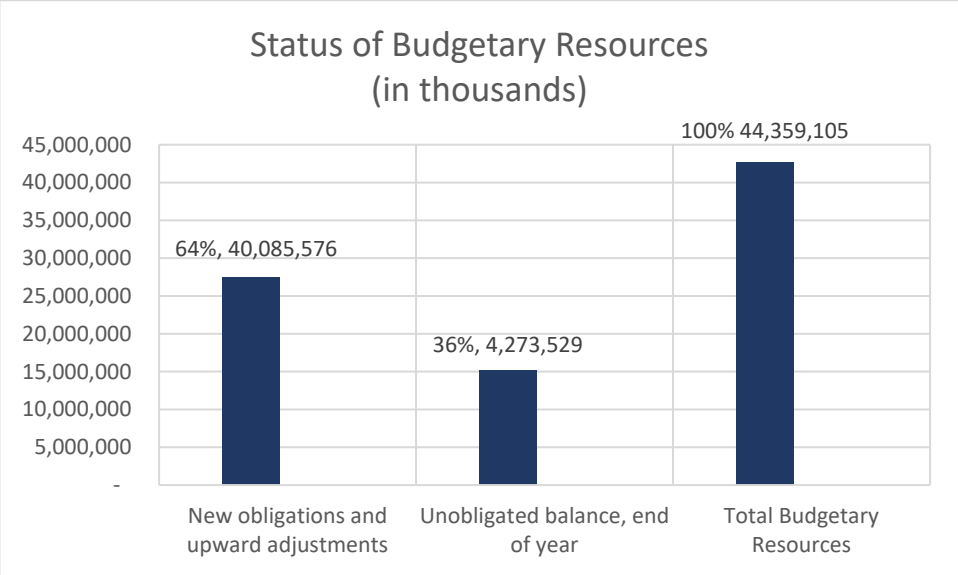


Figure 10 to the left shows the obligations incurred, unobligated balances, and total budgetary resources for DHP for as of September 30, 2019. The DHP has received $44.4 billion, in cumulative budgetary resources as of September 30, 2019, of which it has obligated $40.1 billion, to date.

Obligations and Net Outlays

The status of budgetary resources (Figure 10) shown above shows the overall total budgetary resources received and whether obligations were incurred, or the funding remains in unobligated balances at September 30, 2019. As shown in the chart, the DHP's total budgetary resources as of September 30, 2019 was $44.4 billion. The net outlays for the DHP as of September 30, 2019 is $34.4 billion.

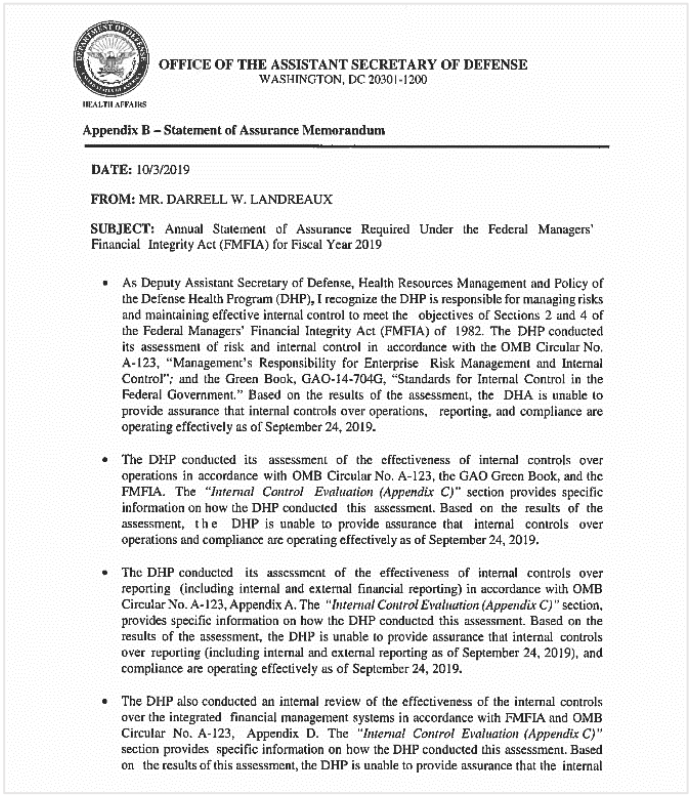
The Department of Defense (DoD) and Labor, Health and Human Services, and Education Appropriations Act, 2019 and Continuing Appropriations Act, 2019, H.R. 6157, P.L. 115-245, was signed by the President on September 28, 2018. The Appropriations Act provided FY 2019 funding for the DoD despite a lapse of appropriation in other parts of the Federal Government. During the second quarter Private Sector Claims increased unexpectedly, driving reprogramming of other funding within the Defense Health Program to cover the requirement. The biggest risk associated with the reprogramming was the potential delay in facility restoration and modernization projects. While this risk was unwelcome, it was necessary in order to fund healthcare claims that there is a legal requirement to pay

Analysis of Systems, Controls, and Legal Compliance

The DHP management is required to comply with various laws and regulations in establishing, maintaining, and monitoring internal controls over operations (ICO), financial reporting, and financial management systems as discussed below.

Management Assurances

The Assurance Statements below were provided for FY 2019 Federal Manager's Financial Integrity Act for FY 2019 (FMFIA).



OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE
WASHINGTON, DC 20301-1200

HEALTH AFFAIRS

Appendix B – Statement of Assurance Memorandum

DATE: 10/3/2019

FROM: MR. DARRELL W. LANDREAUX

SUBJECT: Annual Statement of Assurance Required Under the Federal Managers' Financial Integrity Act (FMFIA) for Fiscal Year 2019

- As Deputy Assistant Secretary of Defense, Health Resources Management and Policy of the Defense Health Program (DHP), I recognize the DHP is responsible for managing risks and maintaining effective internal control to meet the objectives of Sections 2 and 4 of the Federal Managers' Financial Integrity Act (FMFIA) of 1982. The DHP conducted its assessment of risk and internal control in accordance with the OMB Circular No. A-123, "Management's Responsibility for Enterprise Risk Management and Internal Control"; and the Green Book, GAO-14-704G, "Standards for Internal Control in the Federal Government." Based on the results of the assessment, the DHA is unable to provide assurance that internal controls over operations, reporting, and compliance are operating effectively as of September 24, 2019.

- The DHP conducted its assessment of the effectiveness of internal controls over operations in accordance with OMB Circular No. A-123, the GAO Green Book, and the FMFIA. The *"Internal Control Evaluation (Appendix C)"* section provides specific information on how the DHP conducted this assessment. Based on the results of the assessment, the DHP is unable to provide assurance that internal controls over operations and compliance are operating effectively as of September 24, 2019.

- The DHP conducted its assessment of the effectiveness of internal controls over reporting (including internal and external financial reporting) in accordance with OMB Circular No. A-123, Appendix A. The *"Internal Control Evaluation (Appendix C)"* section, provides specific information on how the DHP conducted this assessment. Based on the results of the assessment, the DHP is unable to provide assurance that internal controls over reporting (including internal and external reporting as of September 24, 2019), and compliance are operating effectively as of September 24, 2019.

- The DHP also conducted an internal review of the effectiveness of the internal controls over the integrated financial management systems in accordance with FMFIA and OMB Circular No. A-123, Appendix D. The *"Internal Control Evaluation (Appendix C)"* section provides specific information on how the DHP conducted this assessment. Based on the results of this assessment, the DHP is unable to provide assurance that the internal controls over the financial systems are in compliance with the FMFIA, Section 4; FFMIA, Section 803; and OMB Circular No. A-123, Appendix D, as of September 24, 2019.

- The DHP has conducted an assessment of entity-level controls including fraud controls in accordance with the Green Book, OMB Circular No. A-123, the Fraud Reduction and Data Analytics Act (FRDAA) of 2015, and GAO Fraud Risk Management Framework. Based on the results of the assessment, the DHP is unable to provide assurance that entity-level controls including fraud controls are operating effectively as of September 24, 2019.

Signed

Darrell W. Landreaux
Deputy Assistant Secretary of Defense
Health Resources Management and Policy

Attachments:
1. Appendix C – Description of the Concept of Reasonable Assurance
2. Appendix D – Significant Deficiencies and Material Weaknesses
3. Appendix E – Material Weakness Removal Memorandum
4. Appendix F – Risk Assessment
5. Appendix G – Significant Managers' Internal Control Program Accomplishments
6. Appendix H – Entity Level and Fraud Control Checklist
7. Appendix K - DHP Component/Service Medical Activities Statement of Assurance

Summary of Internal Control Assessment

The DHP conducted its assessment of the effectiveness of ICO in accordance with the FMFIA and the Office of Management and Budget (OMB) Circular No. A-123 *Management's Responsibility for Enterprise Risk Management and Internal Control*. Each evaluation occurred at the component level and was reported to the DHP with the results and testing methodology used to evaluate the status of the control. Based on the results of the assessment, the DHP is unable to provide assurance that ICO, reporting, and compliance were operating effectively as of September 30, 2019.

The DHP assessed the effectiveness of internal controls over financial reporting (ICOFR), including external financial reporting, in accordance with OMB Circular No. A-123, Appendix A, *Internal Control over Financial Report*. Each evaluation occurred at the component level and was reported to the DHP with the results and testing methodology used to evaluate the status of the control. Based on the results of the assessment, the DHP is unable to provide assurance that internal controls over reporting were operating effectively as of September 30, 2019.

The DHP also conducted an internal review of the effectiveness of internal controls over the financial systems (ICOFS) in accordance with FFMIA of 1996 (Public Law 104-208) and OMB Circular No. A-123, Appendix D. Each evaluation occurred at the component level and was reported to DHP with the results and testing methodology used to evaluate the status of the control. Based on the results of the assessment, the DHP is unable to provide assurance that ICOFS are in compliance with FFMIA and OMB Circular No. A-123, Appendix D, *Compliance with the Federal Financial Management Improvement Act (FFMIA) of 1996* as of September 30, 2019.

The DHP Managers Internal Control Program (MICP) is focused on refining and improving the Enterprise Level Controls (ELCs) in FY 2019 and FY 2020. Correcting design failures and strengthening the ELCs should help the Enterprise improve control and oversight over operations, reporting, and compliance. An Enterprise communication plan is being developed to ensure all responsible parties are aware of their roles related to specific ELCs. This two-pronged effort should improve the effectiveness of the controls.

Management's assessment of FFMIA compliance was completed prior to the results of the FY 2019 financial statement audit. Our auditor has noted the DHP financial management systems did not comply with the federal financial management system's requirements, applicable federal accounting standards, or application of the United States Standard General Ledger (USSGL) at the transaction level, because of material weaknesses noted in the Independent Auditor's Report on Internal Control over Financial Reporting. The DHP is in the process of evaluating the FY 2019 audit findings contributing to noncompliance to begin the process of formulating remediation plans necessary to bring the financial management systems into substantial compliance.

Compliance with Laws and Regulations

Anti-Deficiency Act (ADA), 31 U.S.C. §§ 1341, 1342, 1350, 1351, 1517

The ADA prohibits federal employees from obligating in excess of an appropriation, before funds are available or from accepting voluntary services. As required by the ADA, DHP notifies all appropriate authorities of any ADA violations. The DHP management has taken and continues to take necessary steps to prevent ADA violations. Investigations of any violations will be completed in a thorough and expedient manner. DHP remains fully committed to resolving ADA violations appropriately and in compliance with all aspects of the law.

Pay and Allowance System for Civilian Employees as provided in 5 U.S.C. Chapters 51–59

5 U.S.C. Chapters 51–59 codify the statutory provisions concerning the pay and allowances afforded federal employees. DHP is fully committed to complying with these provisions, periodically reviewing its compliance with them, and taking appropriate action to achieve compliance if and when any errors are identified. ***Link to 5 U.S.C Chapter 51:***

https://www.gpo.gov/fdsys/granule/USCODE-2011-title5/USCODE-2011-title5-partIII-subpartD-chap51/content-detail.html

Prompt Payment Act, 31 U.S.C. §§ 3901–3907

In 1982, Congress enacted the Prompt Payment Act (PPA) to require federal agencies to pay their bills on a timely basis, to pay interest penalties when payments are made late, and to take discounts only when payments are made by the discount date. DHP uses the Invoice Receipt, Acceptance and Property Transfer (iRAPT) (formerly Wide Area Workflow) system to ensure compliance with this statutory requirement.

Provisions Governing Claims of the United States Government as provided in 31 U.S.C. §§ 3711-3720E (including provisions of the Debt Collection Improvement Act of 1996, (DCIA), as amended by the Digital Accountability and Transparency Act (DATA Act) of 2014)

The DCIA, as amended by the DATA Act, requires that Federal agencies refer delinquent debts to Treasury within 120 days and take all appropriate steps prior to discharging debts. DHP follows applicable requirements for establishing and collecting validated debts and ensuring compliance with Debt Collection statutes and regulations.

However, in FY 2019 SMA-Army reported a material weakness on Medical Delinquent Debt Management; (a) lack of compliance with financial regulations with respect to det management, including requirements associated with transfer of debt, timeliness, and debt assignment, and (b) information systems support for Uniform Billing Office (UBO) processes.

Government Charge Card Abuse Prevention Act of 2012, Pub. L. No. 112-194

The Charge Card Abuse Prevention Act (Charge Card Act) requires agencies to establish and maintain safeguards and internal controls for purchase cards, travel cards, integrated cards, and centrally billed accounts. Furthermore, the Charge Card Act requires agencies to report purchase card violations, and the IG to conduct periodic risk assessments of government charge card programs. DHP, through implemented internal controls, is committed to continued compliance with all aspects of the public law.

Federal Information Security Modernization Act (FISMA) of 2014

The FISMA requires agencies to report major information security incidents as well as data breaches to Congress as they occur and annually and simplifies existing FISMA reporting to eliminate inefficient or wasteful reporting while adding new requirements for major information security incidents.

In FY 2019 DHP was not in compliance with FISMA due to the several identified deviations from NIST standards and guidelines.

Federal Financial Management Improvement Act (FFMIA) of 1996

The FFMIA requires agencies to implement and maintain financial systems that comply substantially with Federal Financial System (FFS) requirements, applicable federal accounting standards, and the USSGL at the transaction level.

In FY 2019 the DHP's financial management systems do not substantially comply with the requirements within FFMIA, as asserted to by management due to the asserted departures from GAAP and USSGL requirements.

DATA Act, 31 U.S.C. § 6101 note. The DATA Act amended the Federal Funding Accountability and Transparency Act of 2006 (FFATA). DIGITAL ACCOUNTABILITY AND TRANSPARENCY ACT OF 2014

The DATA Act expands the FFATA to increase accountability and transparency in federal spending, making federal expenditure information more accessible to the public. It directs the Federal Government to use government-wide data standards for developing and publishing reports and to make more information, including award-related data, available on the USASpending.gov Web site. The standards and Web site allow stakeholders to track federal spending more effectively. Among other goals, the DATA Act aims to improve the quality of the information on USASpending.gov, as verified through regular audits of the posted data, and to streamline and simplify reporting requirements through clear data standards. DHP complies with the DATA Act; making its expenditures accessible to the public on USASpending.gov.

In addition to compliance with the original legislation and subsequent guidance from OMB over the DATA Act, a revised Appendix A to Circular A-123 was released in June 2018. The revised Appendix was accompanied with a cover letter that requires DATA ACT reporting agencies to create Data Quality Plans. Consideration of this plan must be included in agencies' existing annual assurance statement for internal controls over reporting beginning in FY 2019 and continuing through the assurance statement covering FY 2021 at a minimum or until agencies determine that they can provide reasonable assurance over the data quality controls that support achievement of the reporting objectives in accordance with the DATA ACT.

Grants Oversight and New Efficiency Act

The Grants Oversight and New Efficiency (GONE) Act requires the head of each agency to submit to Congress, in coordination with the Secretary of Health and Human Services, a report on Federal grant cooperative agreement awards that have not yet been closed out and for which the period of performance, including any extensions, elapsed for more than two years. The GONE Act also sets forth follow-on reporting and analysis requirements by various entities."

Healthcare services incurred on behalf of covered beneficiaries: collection from third-party payers as provided in 10 U.S.C. § 1095

Title 10, United States Code (U.S.C.), Section 1095 authorizes MTFs to recover the cost of providing healthcare services to covered DoD beneficiaries from third party payers. The Third-Party Collection Program (TPCP) is the military program established to accomplish this task.

Financial Systems Framework

Financial Management Systems Strategy

The FY 2017 NDAA has called for the reform of the MHS and MTFs. According to Section 702 of the FY 2017 NDAA,

"*Beginning on October 1, 2018 the Director of the DHA shall be responsible for the administration of each MTF, including with respect to budgetary matters, IT, healthcare administration and management, administrative policy and procedure, military medical construction, and any other matters the Secretary of Defense determines appropriate*."

The rationale behind this legislation revolves around the strength of a centralized organization serving the medical needs of all branches of the military. In the prior state, despite having a common funding source, the individual MHS components operated on separate accounting systems. This arrangement made it difficult to get comparable financial data and hindered leadership from making well-informed decisions. It also complicates audit preparation, as the DHP appropriation is undergoing audit as a single entity. In an effort to adhere to the FY 2017 NDAA, to enhance auditability, and provide seamless medical care across all services, the ASD(HA) has decided to work towards a single accounting system solution.

The ASD(HA)'s FY 2017 NDAA compliance strategy is being executed by using a single accounting solution, General Fund Enterprise Business System (GFEBS). This commercial, off the shelf Enterprise Resource Planning (ERP) software tool built on Systems Applications and Products (SAP) implemented by the U.S. Army provides financial information in real time and reveals cost drivers to provide decision support information for leadership. It is a fully open system that allows transparency across all Army, NCR (now tIMO), FOD and USUHS for better visibility and in turn better accountability of our funds. GFEBS is a modern ERP with inherent "best practices" and is commercially maintained and updated. GFEBS also provides analytics data and tools, reduces the cost of business operations, and improves accountability. The system will enable the Army to meet congressional mandates, requiring audit compliance and an accurate accounting of all financial transactions, and will allow the DHP to meet similar requirements and needs.

MEDCOM implemented GFEBS in FY 2010, and in FY 2015, a proof of concept GFEBS deployment to the NCR Medical Directorate (MD) (now tIMO), to include WRNMMC was executed. The notable factor of this implementation was WRNMMC's classification as a Navy chassis. This implementation effectively illustrated the ability of a non-Army entity to successfully deploy GFEBS. With MEDCOM and NCR MD on GFEBS, some of the DHP funding was accounted for in this single system. Following the resounding success of this proof of concept, leadership became interested in pursuing a system-wide deployment in a realistic, sequential manner that would bring the remaining balance of the DHP funding on GFEBS.

The DHA-FOD and USUHS deployed GFEBS on April 2, 2018 and plans are currently in place to transition the BUMED next with a phased implementation plan, which will commence in Quarter 1 (Q1) of FY 2020 and conclude in Q4 of FY 2020. For these and other future deployments, the ASD(HA) has agreed to deploy GFEBS "as-is" with basic Army functionality.

In addition to GFEBS, DHP utilizes the following General Ledger (GL) systems: Defense Agencies Initiative (DAI) Legacy System, Defense Enterprise Accounting and Management System (DEAMS), General Accounting and Finance System - Reengineered (GAFS-R), and Standard Accounting and Reporting System - Field Level (STARS-FL).

DEAMS is a Major Automated Information System (MAIS) that uses COTS ERP software to provide accounting and management services for the SMA Air Force. DEAMS is intended to improve financial accountability by providing a single, standard, automated financial management system that is compliant with the Chief Financial Officers Act of 1990 and other mandates. DEAMS performs the following core accounting functions: Core Financial System Management, General Ledger Management, Funds Management, Payment Management, Receivable Management, Cost Management, and Reporting.

GAFS-R is a system that extends the capabilities of the accounting systems that are used by DFAS Columbus to manage, account for, and report status of funds allocated to the U.S. Air Force. GAFS-R includes transaction-level accounting data.

STARS-FL is a general fund accounting system that supports finance, accounting, and reporting requirements for both field-level and major command headquarters.

In addition to the GL systems, DHA owns four (4) financially relevant feeder systems: Armed Forces Billing and Collection Utilization Solution (ABACUS), Coding and Compliance Editor (CCE), Composite Health Care System (CHCS), and Defense Medical Logistics Standard Support (DMLSS). DHA also relies on service provider feeder systems. For service provider systems, DHP obtains System and Organization Controls (SOC 1) reports. DHA implements Complementary User Entity Controls (CUECs) identified in SOC 1 reports to address control objectives specified in management's description of the service provider system.

Current and Future Financial Management Systems Framework

Due to the FY 2017 NDAA's intent in driving the DHP towards standardized business practices to help achieve auditability through a single, system-wide accounting solution, it is important that the MHS aligns common interests and interacts with Army as "one voice." This new protocol will apply to communication with Army regarding the GFEBS Functional Governance Board (FGB) for requesting system enhancements, the Army GFEBS Process Owners Group (POG) and audit support requests from Army. As MHS' use of GFEBS matures, the one-voice protocol may expand into additional areas. It is important to note here that this will be a marked departure from the previous "way of life" for organizations such as MEDCOM and NCR MD and an entirely new process for DHA-FOD, USUHS, and BUMED.

Prior to the one-voice initiative, MEDCOM was one of the commands represented as a stand-alone advisory member at the Army FGB; however, MEDCOM and all other organizations under the purview of the DHP per the 2017 NDAA will now be represented by the ASD(HA)'s designated department defined below. To cover the requirements in this new environment, organizations such as NCR MD (now tIMO), MEDCOM, and others must speak with one voice when submitting requests to Army regarding GFEBS.

In a concerted effort to consolidate the varying voices of MHS into a single, focused entity, the Health Affairs Functional Champion (HAFC) will represent MHS at GFEBS FGB meetings as an FGB Advisory Member and at POG meetings. Prior to the escalation of issues to GFEBS FGB's Voting Members for official consideration, an internal DHP process will be established to identify, validate, and set priorities for GFEBS enhancements used by for the MHS. This process will identify MHS priorities while also highlighting audit compliance and cost savings/avoidance where applicable. The process will be initiated through HAFC's own Governance Board as the first step in submission to GFEBS FGB. Once the prioritization is made within HAFC and an FGB Voting Member has sponsored the case (by Army FGB rules, all cases brought forth require sponsorship by a GFEBS FGB Voting Member), the various MHS cases from the field will exit HAFC's vetting process and officially enter GFEBS FGB's consideration phase for discussion and an eventual vote.

This consolidation of MHS as required by the FY 2017 NDAA will strengthen MHS by uniting such a large, joint force community with uniquely converging interests into one focused voice. Prior to the legislation, MHS faced potential challenges as voices of the MHS community could be overlooked as the requirement would impact fewer users. With a united voice, MHS will be able to clearly and effectively organize and effect change when necessary and to obtain clear guidance from HAFC when needed, while eliminating the risk of duplicated work efforts of a fragmented MHS community.

Forward-Looking Information

Changes and the Future of the MHS

For FY 2020, the driving forces for the MHS will continue to be on reform of the MHS, reform of the TRICARE benefit, and transformation of the MHS.

MHS Transformation

The focus of the MHS transformation is on Section 702 of the NDAA of FY 2017. This is one of the largest organizational changes within the MHS within recent decades. The end-state is to further the Quadruple Aim of Increased Readiness, Better Care, Better Health, and Lower Cost. The Quadruple Aim has developed strategic goals that allow all military services to prioritize its portfolio of work and ensure the proper alignment of resources. All MTFs will utilize the Quadruple Aim Performance Process (QPP), by creating, acquiring, and transferring new knowledge to achieve breakthrough performance.

- The NDAA's objectives will be accomplished with the framework of the Quadruple Aim and the execution of the QPP.
- The integration of varied approaches to the health system optimization into one enterprise ensures MHS' readiness.
- The execution of the QPP allows the DHA and the military services to optimize and deliver the Quadruple Aim to address the NDAA reforms.

Execution for the MTF transition will provide maximized efficiency (eliminating redundancies) across the landscape, addresses DoD's medical readiness requirements, provides better consistency of higher quality experience, and most importantly, reduces enterprise operational costs. The authority, direction, and control of MTFs will be managed under a market construct, which is designed to leverage and expand on the existing enhanced Multi-Service Market (eMSM) concept to scale optimization and efficiencies across the MHS.

- The Market Construct will drive process standardization, reduce variability, and generate efficiencies and optimization across the MHS.
- Sustain a world-class health care system by providing health care services based on population health care demands
- Improve decision-making and execution for improved patient care and experience.
- Effect the enterprise culture, enhancing both operations and delivery of care.

While numerous advantages lay ahead for administration and management of through a market-based lens, there are undoubtedly risks that require acknowledgement. The standup and certification of each market presents some risk. This risk is largely mitigated as each market standup is conditions-based rather than time-based. In the unlikely event a market is not initiated or cannot attain certification (after the market is stood up), the MHS transformation could lose momentum and wide variation in administrative processes remain.

TRICARE Benefits

The implementation of TRICARE Select in January 2018, which replaced TRICARE Standard and TRICARE Extra, was a large change in healthcare benefits. TRICARE Select is a self-managed preferred provided network plan for beneficiaries. Similar to TRICARE Standard, fees for some beneficiary categories exist.

- An annual enrollment fees for some beneficiary categories exist,
- An annual deductible exists,
- Some fixed fees for outpatient services exist, and
- Some cost-sharing exists.

The rising cost of providing healthcare for TRICARE beneficiaries is a risk to the Department. For example, the Congressional Budget Office estimates the average annual costs to provide healthcare for a military retiree and his/her family is $17,800. In terms of out-of-pocket expenses for these retiree families, an equivalent civilian health plan would cost five- to six-times more. Additionally, the rate at which working-age military retirees opt for private health insurance continues to decline – this metric dropped by 12.5% in 2018. To offset these costs, modest fee increases, mainly cost shifting to the beneficiary, is one option to help control the rate of cost increases in healthcare. Although this option remains contested among beneficiaries and military service organizations, few alternatives remain viable to assist in curbing the increasing costs.

MHS GENESIS

The deployment of the MHS' new electronic health record, MHS GENESIS, continues with deployment and implementation in the western United States. These deployment schedules fall on the heels of lessons learned, training enhancements, and modifications to the end-user experience from the initial operating capability (IOC) sites in the Pacific Northwest. The next deployment phases for MHS GENESIS include Wave 1 and Wave 4. Wave 1 includes Mountain Home Air Force Base, Travis Air Force Base, Lemoore, and Monterey (a branch clinic to Madigan Army Medical Center). Wave 4 includes Nellis Air Force Base, Twenty-nine Palms, Fort Irwin, Beale Air Force Base, Port Hueneme, Edwards Air Force Base, Naval Air Station Fallon, Los Angeles Air Force Base, Bridgeport Dental (Mountain Warfare Training Center), and Vandenberg Air Force Base.

The intensive planning and pre-implementation to-date has resulted in near seamless rollout of MHS GENESIS across military sites. The implementation, however, was not without some risks. Cyber-security, provider training, and end-user adoption contributed to some shifts in original IOC timelines (original date was March 2017, revised date was October 2017). To mitigate future risks, and based upon IOC lessons learned, schedule adjustments were made to improve the software, training, and workflow.

Limitations of the Financial Statements

The principal financial statements are prepared to report the financial position and results of operations of DHP, pursuant to the requirements of 31 U.S.C. § 3515(b). The statements are prepared from the books and records Federal entities in accordance with Federal Generally Accepted Accounting Principles (GAAP) and formats prescribed by OMB. Reports used to monitor, and control budgetary resources are prepared from the same books and records. The financial statements should be read with the realization that they are for a component of the U.S. Government.

II. Financial Section

Office of the Inspector General Transmittal

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
4800 MARK CENTER DRIVE
ALEXANDRIA, VIRGINIA 22350-1500

November 8, 2019

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)/CHIEF FINANCIAL OFFICER, DOD
ASSISTANT SECRETARY OF DEFENSE (HEALTH AFFAIRS)
DIRECTOR, DEFENSE FINANCE AND ACCOUNTING SERVICE

SUBJECT: Transmittal of the Independent Auditor's Reports on the Defense Health Program Enterprise Financial Statements and Related Notes for FY 2019 and FY 2018 (Project No. D2019-D000FT-0094.000, Report No. DODIG-2020-018)

We contracted with the independent public accounting firm of Kearney & Company to audit the Defense Health Program (DHP) Enterprise Financial Statements and related notes as of and for the fiscal years ended September 30, 2019, and 2018. The contract required Kearney & Company to provide a report on internal control over financial reporting and compliance with laws and other matters, and to report on whether the DHP's financial management systems did not substantially comply with the requirements of the Federal Financial Management Improvement Act of 1996 (FFMIA). The contract required Kearney & Company to conduct the audit in accordance with generally accepted government auditing standards (GAGAS); Office of Management and Budget audit guidance; and the Government Accountability Office/Council of the Inspectors General on Integrity and Efficiency "Financial Audit Manual," June 2018. Kearney & Company's Independent Auditor's Reports are attached.

Kearney & Company's audit resulted in a disclaimer of opinion. Kearney & Company could not obtain sufficient, appropriate audit evidence to support the reported amounts within the DHP financial statements. As a result, Kearney & Company could not conclude whether the financial statements and related notes were presented fairly in accordance with generally accepted accounting principles. Accordingly, Kearney & Company did not express an opinion on the DHP Enterprise FY 2019 and FY 2018 Financial Statements and related notes.

Kearney & Company's separate report, "Independent Auditor's Report on Internal Control Over Financial Reporting," discusses 13 material weaknesses related to the DHP's internal controls over financial reporting.* Specifically, Kearney & Company's report describes the following significant matters:

- The DHP did not have an effective enterprise-level accounting and financial reporting governance and oversight organization to achieve its accounting and financial reporting objectives and responsibilities and did not design a formal process to assess and monitor the adequacy of its components' internal control programs.

- The DHP, in coordination with its service organization, was unable to completely reconcile its universe of transactions from the general ledger system trial balance through to the final DHP financial statements.

- The DHP did not exercise oversight of its components and its service organization to enforce the generation and retention of supporting documentation to maintain an audit trail which resulted in the DHP's financial statements containing material unsupported journal voucher adjustments.

- The DHP, in coordination with its service organization, did not design all necessary internal control activities or document its end-to-end Fund Balance with Treasury reporting and reconciliation process and experienced problems regarding accuracy and completeness of collections and disbursements related to Fund Balance with Treasury.

- The DHP components did not consistently account for revenue or accounts receivable resulting from medical services provided. In addition, the DHP has not implemented effective medical coding procedures to ensure the accuracy of medical coding applied over inpatient, outpatient, ambulatory procedure visit, and inpatient professional service healthcare encounters.

- The DHP did not record General Equipment in a consistent manner and did not completely implement policies, procedures, or internal controls to identify, recognize, and report General Equipment for all components.

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* A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting that results in a reasonable possibility that management will not prevent, or detect and correct, a material misstatement in the financial statements in a timely manner.

- The DHP did not value its Property, Plant, and Equipment at historical cost and did not use alternative valuation methodologies in accordance with generally accepted accounting principles.

- The DHP did not record Real Property as part of the Property, Plant, and Equipment balance and the DHP components did not appropriately apply capitalization policies to real property construction in progress projects funded by Operation and Maintenance funds.

- The DHP did not begin valuation efforts over internal use software using alternative valuation methodologies and it was unable to value internal use software at historical cost in accordance with generally accepted accounting principles.

- The DHP did not perform an assessment of Operating Material and Supplies to determine the appropriate accounting treatment in accordance with generally accepted accounting principles. In addition, the DHP components did not account for stockpile material in accordance with generally accepted accounting principles.

- The DHP did not design and implement effective internal controls within respective procurement processes to ensure goods and services received but not yet paid for are appropriately accrued.

- The DHP's internal controls were not operating effectively to review, assess, and close stale obligations on a timely basis or has not been fully implemented across all components.

- The DHP had control deficiencies in the design, implementation, and operating effectiveness of internal controls related to financially significant systems to include access controls.

Kearney & Company's additional report, "Independent Auditor's Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements," discusses four instances of noncompliance with applicable laws and regulations and one potential violation of the Antideficiency Act. Specifically, Kearney & Company's report described instances where DHP did not comply with the Federal Managers' Financial Integrity Act, the Federal Information Security Modernization Act, the FFMIA, and the Debt Collection Improvement Act.

In connection with the contract, we reviewed Kearney & Company's reports and related documentation and discussed them with Kearney & Company's representatives. Our review, as differentiated from an audit of the financial statements in accordance with GAGAS, was not intended to enable us to express, and we do not express, an opinion on the DHP Enterprise FY 2019 and FY 2018 Financial Statements and related notes, conclusions about the effectiveness of internal control over financial reporting, or conclusions on whether the DHP's financial systems substantially complied with FFMIA requirements, or on compliance with laws and other matters. Our review disclosed no instances where Kearney & Company did not comply, in all material respects, with GAGAS. Kearney & Company is responsible for the attached reports, dated November 8, 2019, and the conclusions expressed within the reports.

We appreciate the cooperation and assistance received during the audit. Please direct questions to me.

Signed

Lorin T. Venable, CPA
Assistant Inspector General for Audit
Financial Management and Reporting

Attachments:
As stated

Independent Auditor's Report

KEARNEY& COMPANY

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INDEPENDENT AUDITOR'S REPORT

To the Assistant Secretary of Defense for Health Affairs and Inspector General of the Department of Defense

Report on the Financial Statements

We were engaged to audit the accompanying consolidated financial statements of the Defense Health Program (DHP) Enterprise (hereinafter referred to as the DHP), which comprise the consolidated balance sheets as of September 30, 2019 and 2018, the related consolidated statements of net cost and changes in net position, and the combined statements of budgetary resources (hereinafter referred to as the "financial statements") for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on conducting the audits in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 19-03, *Audit Requirements for Federal Financial Statements*. Because of the matters described in the Basis for Disclaimer of Opinion section below, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for Disclaimer of Opinion

We were unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion that the financial statements are free from material misstatements when taken as a whole. The DHP disclosed in Note 1, *Significant Accounting Policies*, instances where its current accounting and business practices represent departures from accounting principles generally accepted in the United States of America. As a result, the DHP was unable to assert that the financial statements are presented fairly in accordance with accounting principles generally accepted in the United States of America. The DHP asserted to the following departures from accounting principles generally accepted in the United States of America:

KEARNEY& COMPANY

- Accrual accounting requirements per Statement of Federal Financial Accounting Standards (SFFAS) No. 1, *Accounting for Selected Assets and Liabilities*, and SFFAS No. 5, *Accounting for Liabilities of The Federal Government*
- Recognition and valuation requirements set forth in SFFAS No. 3, *Accounting for Inventory and Related Property*
- Liability requirements set forth in SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, and SFFAS No. 12, *Recognition of Contingent Liabilities Arising from Litigation*
- Recognition and valuation requirements set forth in SFFAS No. 6, *Accounting for Property, Plant, and Equipment*
- Revenue recognition requirements set forth in SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*
- Recognition and valuation requirements set forth in SFFAS No. 10, *Accounting for Internal Use Software*
- Reporting and valuation requirements set forth in SFFAS No. 29, *Heritage Assets and Stewardship Land*
- The full cost provisions of SFFAS No. 4, *Managerial Cost Accounting Standards and Concepts*, as amended by SFFAS No. 55, *Amending Inter-Entity Cost Provisions*
- Accounting and reporting requirements associated with deposit fund activity per SFFAS No. 31, *Accounting for Fiduciary Activities*
- Reporting requirements set forth in SFFAS No. 42, *Deferred Maintenance and Repairs: Amending Statements of Federal Financial Accounting Standards 6, 14, 29, and 32*.

We were unable to obtain sufficient appropriate evidential matter as to the completeness of the financial statements reported as of September 30, 2019. This includes $19.6 billion of Fund Balance with Treasury (FBWT), $1.1 billion of Accounts Payable ($183.7 million Federal and $932.6 million Non-Federal), $184.9 million in Other Liabilities ($98.8 million Federal and $86.1 million Non-Federal), and $18.1 million in Environmental and Disposal Liabilities balances on the balance sheet.

We were unable to obtain sufficient appropriate evidential matter to enable us to perform audit procedures to support the completeness and accuracy of the financial statements in accordance with accounting principles generally accepted in the United States of America and Department of the Treasury (Treasury) standard general ledger reporting requirements. The DHP is unable to reconcile its financial statements to supporting general ledger (GL) system trial balances and GL system transaction details without material variances. The DHP and its financial reporting service organization are unable to support, and do not have underlying transaction-level data available for, material adjustments recorded during the financial statement compilation process.

We were unable to obtain sufficient appropriate evidential matter as to the existence, completeness, and accuracy of the DHP's stockpile material reported within the Inventory and Related Property line item of the balance sheet. As of September 30, 2019, the DHP reported approximately $52.1 million of Inventory and Related Property on the balance sheet, consisting solely of stockpile material. The DHP did not record stockpile material in accordance with

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SFFAS No. 3. The DHP was unable to provide sufficient data to allow audit procedures to be performed over the existence, completeness, and valuation of stockpile material. In addition, the DHP has not performed the required assessment for Operating Materials and Supplies (OM&S) to support its accounting treatment selected under SFFAS No. 3. The DHP did not report OM&S within the Inventory and Related Property line item of the balance sheet, directly expensing OM&S upon purchase. The DHP was unable to provide sufficient evidence to support that this method of accounting was appropriate based on prescribed conditions within SFFAS No. 3.

We were unable to obtain sufficient appropriate evidential matter to enable us to perform audit procedures to satisfy ourselves that the Property, Plant, and Equipment (PP&E) opening balances as of October 1, 2018 or ending balance balances as of September 30, 2019 were free of material misstatements. Our work identified issues related to existence, completeness, valuation, and disclosure of real property (including real property construction-in-progress [CIP]), internal use software (IUS) (including IUS in development), and general equipment. As of September 30, 2019, the DHP reported $3.2 billion in net PP&E on its balance sheet.

We were unable to obtain sufficient appropriate evidential matter as to the completeness of revenue and associated accounts receivable. The DHP does not account for all revenue and accounts receivable transactions using the accrual basis of accounting, recording certain activity on the cash basis of accounting. As of September 30, 2019, the DHP reported $943.5 million of accounts receivable ($205.7 million Federal and $737.8 million Non-Federal), net on its balance sheet and $3.8 billion of earned revenue on its statement of net cost.

We were unable to obtain audited financial statements of construction funds sub-allotted to the United States Army Corps of Engineers (USACE), supporting the DHP's real property CIP managed by USACE. The DHP reported $2.7 billion of real property CIP as of September 30, 2019, which is included as part of the PP&E, net line item of the balance sheet, and described in Note 7 to the consolidated financial statements.

The effects of the conditions described in the preceding paragraphs cannot be fully quantified, nor was it practical, given the available information, to extend audit procedures to sufficiently determine the extent of the misstatements to the financial statements. The effects of the conditions in the preceding paragraphs and overall challenges in obtaining timely and sufficient audit evidence also made it impractical to execute all planned audit procedures. As a result of these departures, we were unable to determine whether any adjustments might have been found necessary in respect of recorded or unrecorded amounts within the elements of the financial statements.

Disclaimer of Opinion

Because of the significance of the matters described in the Basis for Disclaimer of Opinion section above, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on these financial statements.

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Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that Management's Discussion and Analysis, other Required Supplementary Information, and Required Supplementary Stewardship Information (hereinafter referred to as the "required supplementary information") be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by OMB and the Federal Accounting Standards Advisory Board (FASAB), who consider it to be an essential part of the financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. We were unable to apply certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America because of matters described in the Basis for Disclaimer of Opinion section above. We do not express an opinion or provide any assurance on the information.

Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. Other Information as named in the Agency Financial Report is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audits of the financial statements; accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards* and OMB Bulletin No. 19-03, we have also issued reports, dated November 8, 2019, on our consideration of the DHP's internal control over financial reporting and on our tests of the DHP's compliance with provisions of applicable laws, regulations, contracts, and grant agreements, as well as other matters for the year ended September 30, 2019. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance and other matters. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* and OMB Bulletin No. 19-03 and should be considered in assessing the results of our audit.

Kearney & Company

Alexandria, Virginia
November 8, 2019

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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

To the Assistant Secretary of Defense for Health Affairs and Inspector General of the Department of Defense

We were engaged to audit, in accordance with the auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 19-03, *Audit Requirements for Federal Financial Statements*, the financial statements of the Defense Health Program (DHP) as of and for the year ended September 30, 2019, and the related notes to the financial statements, which collectively comprise the DHP's financial statements, and we have issued our report thereon dated November 8, 2019. Our report disclaims an opinion on such financial statements because we were unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. The DHP also asserted to departures from generally accepted accounting principles.

Internal Control over Financial Reporting

In connection with our engagement to audit the financial statements of the DHP, we considered the DHP's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the DHP's internal control. Accordingly, we do not express an opinion on the effectiveness of the DHP's internal control. We limited our internal control testing to those controls necessary to achieve the objectives described in OMB Bulletin No. 19-03. We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982 (FMFIA), such as those controls relevant to ensuring efficient operations.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies; therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings, we did identify certain deficiencies in internal control that we consider to be material weaknesses.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings to be material weaknesses.

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A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

We noted certain additional matters involving internal control over financial reporting that we will report to the DHP's management in a separate letter.

The DHP's Response to Findings

The DHP's response to the findings identified in our engagement is described in a separate memorandum attached to this report in Section 2, *Financial Section*, of the Agency Financial Report. The DHP's response was not subjected to the auditing procedures applied in the engagement to audit the financial statements, and accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and the results of that testing, and not to provide an opinion on the effectiveness of the DHP's internal control. This report is an integral part of an engagement to perform an audit in accordance with *Government Auditing Standards* and OMB Bulletin No. 19-03 in considering the entity's internal control. Accordingly, this communication is not suitable for any other purpose.

Alexandria, Virginia
November 8, 2019

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Schedule of Findings

Material Weaknesses

The Military Health System (MHS), which is the global health system of the Department of Defense (DoD), is composed of medical personnel, infrastructure, and resources from the Departments of the Army, Navy, and Air Force; the Defense Health Agency (DHA); and the Office of the Assistant Secretary of Defense (Health Affairs). The Defense Health Program (DHP) appropriation serves as a funding source for the MHS. The DHP Enterprise financial statements comprise the following component reporting entities:

- DHA Financial Operations Division (FOD)
- DHA Contract Resource Management (CRM)
- Uniformed Services University of Health Sciences (USUHS)
- Service Medical Activity (SMA) – Army/Army Medical Command (MEDCOM)
- SMA – Navy/Navy Bureau of Medicine and Surgery (BUMED)
- SMA – Air Force (AF)/Air Force Medical Service (AFMS)
- SMA – National Capital Region Medical Directorate (NCR MD).

Throughout the course of our audit work with each DHP component reporting entity, internal control deficiencies were encountered which were considered for the purposes of reporting on internal control over financial reporting for the DHP. The material weaknesses presented in this Schedule of Findings have been formulated based on our determination of how individual control deficiencies, in aggregate, affect internal controls over financial reporting. The table below presents the material weaknesses identified during our audit:

Accounting Area	Material Weakness
Entity-Level Controls	I. Accounting and Financial Reporting Governance and Entity-Level Controls
Financial Reporting	II. Financial Reporting – Universe of Transaction Reconciliations III. Financial Reporting – Defense Departmental Reporting System Adjustments
Fund Balance with Treasury (FBWT)	IV. Fund Balance with Treasury
Accounts Receivable (AR)	V. Medical Revenue and Associated Receivables
Property, Plant, and Equipment (PP&E)	VI. General Equipment Existence and Completeness VII. Valuation of Property, Plant, and Equipment VIII. Real Property IX. Internal Use Software and Internal Use Software In-Development
Inventory and Related Property	X. Operating Materials and Supplies and Stockpile Material

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Accounting Area	Material Weakness
Accounts Payable (AP) and Related Liabilities	XI. Liabilities and Related Expenses
Budgetary Resources	XII. Monitoring and Reporting of Obligations
Information Technology (IT)	XIII. Information Systems

I. Accounting and Financial Reporting Governance and Entity-Level Controls (*Repeat Condition*)

Deficiencies in two related areas define this material weakness:

A. Accounting and Financial Reporting Governance Structure
B. Entity-Level Control (ELC) Design and Operation.

Background: ELCs relate to an entity's control environment, risk assessment processes, information and communication, and monitoring of control effectiveness over time. These controls are enterprise-wide and have a pervasive effect on an entity's internal control system and may include service organizations. The Federal Managers' Financial Integrity Act of 1982 (FMFIA) requires Federal Executive agencies to establish, implement, periodically review, and report on the agency's internal control systems in accordance with the U.S. Government Accountability Office's (GAO) *Standards for Internal Control in the Federal Government* (commonly referred to as the Green Book).

Agencies implement these requirements by considering the guidance provided by Office of Management and Budget (OMB) Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*. The DHP launched its Manager's Internal Control Program (MICP) to support the design, implementation, and maintenance of its system of internal control.

An agency's system of internal control may be dependent upon processes and controls performed by service organizations. A *Report on Controls at a Service Organization Relevant to User Entities' Internal Control over Financial Reporting* (also known as a SOC 1 report) is specifically intended to meet the needs of entities that use service organizations (user entities) in evaluating the effect of the service organization controls on its financial statements. The control objectives stated in the description of the service organization's system cannot be achieved by the service organization alone. Rather, the achievement of the control objectives is dependent on the user entity's implementation of control activities that address the complementary user entity controls (CUEC) as identified within the SOC 1 report.

Beginning October 1, 2018, the National Defense Authorization Act for Fiscal Year (FY) 2017 (NDAA) consolidated the administration of more than 475 hospitals and clinics currently run by the Army, Navy, and Air Force into a centralized management structure within DHA. The transition of administrative responsibility of the Military Treatment Facilities (MTF) to DHA remained in process during FY 2019.

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A. Accounting and Financial Reporting Governance Structure

Condition: The DHP does not have an effective enterprise-level accounting and financial reporting governance and oversight organization to achieve its accounting and financial reporting objectives and responsibilities.

The organizational hierarchy for the DHP components has not been formalized as it pertains to accounting and financial reporting governance. Specifically, SMA components align themselves with their respective Military Departments and have adopted department-specific accounting policies and procedures accordingly. The DHP components were not always responsive to requests made by the DHP or its senior leadership group to provide documentation to support the DHP MICP.

Further, the DHP lacks implemented accounting policy in the following key areas:

- Fund Balance with Treasury (FBWT)
- General Property, Plant, and Equipment (PP&E)
- Inventory and Related Property
- Accounts Receivable (AR) and Associated Revenue
- Accounts Payable (AP)
- Legal Liabilities
- Financial Reporting.

Cause: The DHP financial management organization continued to evolve during FY 2019. However, as of September 30, 2019, the DHP did not yet have the ability to exercise authority and oversight over all DHP components. The DHP did not have an effective oversight structure in place to monitor components' accounting and financial reporting. The individual management of the DHP components, which are responsible for the execution of DHP funding across the Army, Navy, Air Force, DHA, and Health Affairs, operate independently and have not yet effectively merged into a cohesive, formalized accounting and financial reporting governance structure within the DHP.

Effect: Without an effective enterprise-wide financial management governance and oversight organization, inconsistent policies and procedures can lead to unreliable and inaccurate financial information. Further, SMA components frequently revert to guidance from their respective Military Departments, creating greater ambiguity and confusion.

Unclear delegation of authority and lack of organizational structure between the DHP and components results in ineffective implementation and monitoring of financial management policies and operations, control failures, and potential misstatements to the financial statements. Without the ability to implement an effective internal control assessment program, the risk of producing inaccurate financial statements increases.

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The lack of comprehensive enterprise accounting policy for significant business operations of the DHP contributed to departures from Federal accounting standards issued by the Federal Accounting Standards Advisory Board (FASAB), including:

- Accrual accounting requirements per Statement of Federal Financial Accounting Standards (SFFAS) No. 1, *Accounting for Selected Assets and Liabilities*, and SFFAS No. 5, *Accounting for Liabilities of The Federal Government*
- Recognition and valuation requirements set forth in SFFAS No. 3, *Accounting for Inventory and Related Property*
- Liability requirements set forth in SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, and SFFAS No. 12, *Recognition of Contingent Liabilities Arising from Litigation*
- Recognition and valuation requirements set forth in SFFAS No. 6, *Accounting for Property, Plant, and Equipment*
- Revenue recognition requirements set forth in SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*
- Recognition and valuation requirements set forth in SFFAS No. 10, *Accounting for Internal Use Software*
- The full cost provisions of SFFAS No. 4, *Managerial Cost Accounting Standards and Concepts*, as amended by SFFAS No. 55, *Amending Inter-Entity Cost Implementation*.

Recommendations: Kearney & Company, P.C. (Kearney) recommends that the DHP:

1. Develop and distribute an enterprise governance policy or consider expanding the MHS Governance Business Rules to formalize accounting and financial reporting governance for all components of the DHP financial reporting entity. The policy should specifically address financial and accounting governance, policies and procedures at the Enterprise and component level, accountability, and authority. The policy should also address an oversight role for compliance with established policies and procedures across all components of the reporting entity.
2. Perform a gap analysis over current policy and procedures to determine where Enterprise-wide policy needs development or strengthening for overall compliance with GAO Green Book and Generally Accepted Accounting Principles (GAAP).

B. Entity-Level Control Design and Operation

Condition: The DHP did not meet the standards for an effective internal control system, as defined in GAO's Green Book. The DHP identified 94 ELCs, of which 12 were determined to be ineffectively designed. Of the remaining 82 controls deemed effectively designed, remediation efforts remain in process to address 72 operational effectiveness control failures identified in the prior year. The DHP did not achieve any of the 17 GAO Green Book principles across the five components of internal control.

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The DHP has not designed a formal process to assess and monitor the adequacy of its components' internal control programs in support of the DHP Statement of Assurance.

The DHP components have not demonstrated that all CUECs documented within relevant SOC 1 reports have been designed, implemented, and are operating effectively, nor have they assessed that certain CUECs are not applicable to the DHP's end-to-end processes.

Cause: The DHP MICP has not fully assessed or implemented all principles of internal controls in accordance with FMFIA and Green Book requirements in the design and implementation of ELCs, including those controls necessary in the information system environment. Due to DHA's lack of authority, direction, and control over the SMAs, the DHP components continue to operate independently.

The DHP has not completely documented its ELCs to demonstrate that the controls achieve all control objectives and are operating in an integrated manner.

The DHP components have not fully considered the impact of service organizations within their existing control environments. Additionally, the DHP components do not have a formalized process to map and document existing control activities to required CUECs, nor to assess where internal control gaps may exist based on required CUECs, as defined in applicable SOC 1 reports.

The DHP Enterprise monitoring activities of component CUECs, as well as the requirement for implementation of CUECs by the components, has not been formalized in Enterprise policy or procedural instructions. The lack of formal policy, combined with the current organizational structure of the DHP where component reporting entities align themselves with their respective Military Department, have inhibited responsiveness to monitoring activities for CUEC remediation performed by the DHP Enterprise.

Effect: Without an effective ELC program in place, the DHP is susceptible to inefficient and ineffective operations, unreliable financial reporting, and noncompliance with laws and regulations. Incomplete internal control documentation impedes the DHP's ability to monitor the design, implementation, and operating effectiveness of its ELCs over time.

Failure to fully implement external information system CUECs may result in significant control weaknesses that may be overlooked, along with non-achievement of the related control objective(s), thus increasing the risk of inaccurate financial reporting, as well as unauthorized disclosure and modification to applicable systems and data. Specifically, if DHP components have not implemented CUECs or assessed CUECs for operating effectiveness, then DHP components are unable to sufficiently assess the risk to applicable financial reporting processes impacted by the service organization.

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Recommendations: Kearney recommends that the DHP establish an Enterprise policy for the MICP that requires, at a minimum, the development of ELCs at the DHP and component levels that align with the DHP MICP. The policy should require both the DHP and individual components to:

1. Review Green Book standards and accompanying implementation guidance to design Enterprise-wide ELCs to be implemented at the DHP and component levels.
2. Perform a data call with each of the components to establish an understanding of the following:
   a. Component points of contact (POC).
   b. Key supporting documents, policies, and references identified within the components' current ELCs.
   c. Current programs, functions, and responsibilities to support the agency's compliance with the Green Book.
3. Update assessment criteria based on OMB Circular A-123, best practices, and knowledge of agency operations.
4. Develop a risk assessment model for ELCs, considering work performed under the agency's Enterprise Risk Management (ERM) effort and the Green Book's principles.
5. Review FY 2018 and FY 2019 results and final test plans; update control activity inventory through the annual risk assessment process, hold understanding meetings with DHP ELC POCs, and review existing agency documentation; and crosswalk the documented controls to the respective principle in DHP-approved templates.
6. Document identified instances of control gaps based on design assessment; evaluate the magnitude of impact, likelihood of occurrence, and nature of each deficiency; and develop recommendations for compliance and/or improvement.
7. Design standard templates that are updated to support the assessment strategy and document results at the principle and component levels to provide sufficient evidence to support the effective operation of internal controls.
8. Document and implement policies and procedures for the monitoring of third-party service organization controls in accordance with the Green Book, as well as National Institute of Standards and Technology (NIST) Special Publications (SP) 800-53, *Security and Privacy Controls for Federal Information Systems and Organizations*, and NIST SP 800-35, *Guide to Information Technology Security Services*.
9. Perform timely assessments of DHP control activities for addressing CUECs to determine their applicability to the DHP's internal controls and retain related support in coordination with the risk assessments and the design of internal controls for its end-to-end processes.
10. For CUECs determined to be applicable:
    a. Ensure component reporting entities map CUECs to controls.
    b. Document the design and implementation of the control(s).
    c. Revisit relevant business process documentation to verify inclusion of CUECs.
    d. Test the control(s) to determine whether it is operating as designed.
11. Establish routine communications with the DHP and component service organization(s) to improve awareness of changes to CUECs and potential exceptions that may be reported in the SOC 1 report. This should enable the DHP to timely mitigate risks to its

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financial reporting (i.e., deficiencies within its service organization's controls and related processes). The DHP should also develop methods to document these communications and the changes to the design and implementation of internal controls in response to service organization updates.

II. Financial Reporting – Universe of Transaction Reconciliations (*Repeat Condition*)

Background: The DHP operates in a non-integrated systems environment with financial information from many systems feeding into various DHP component general ledger (GL) systems. DHP financial data is captured within component GL systems from several feeder systems. Monthly, the DHP's service organization transfers feeder files from the component GL systems to Defense Departmental Reporting System – Budgetary (DDRS-B). The transmitted data from each GL system undergoes a series of translations referred to as pre-processing. Quarterly, the DDRS-B data transfers to DDRS – Audited Financial Statements (AFS).

In FY 2019, the DHP, in coordination with the Office of the Under Secretary of Defense (Comptroller) (OUSD[C]), performed a universe of transaction (UoT) compilation and reconciliation process using OUSD(C)'s Advanced Analytics (ADVANA). The DHP, using ADVANA, performs financial statement reconciliation procedures to verify that complete transaction universes are available in support of the compiled financial statements. The overall reconciliation process includes reconciliation points to attempt to support the overall compilation of the DHP's financial statements from component GL systems to DDRS-B and to DDRS-AFS. The UoT reconciliation process consists of four separate reconciliations for each component and three additional reconciliations at the DHP level.

With the exception of DHA-CRM, all of the DHP's components have been included in the UoT reconciliation process. DHA-CRM receives a standalone audit and, therefore, is not included in the UoT reconciliation process. The six DHP components included in ADVANA utilize seven GL systems.

Condition: The DHP, in coordination with its service organizations, was unable to completely reconcile its UoT from the GL system trial balance (TB) through to the final DHP financial statements. The DHP could not sufficiently explain material variances between GL transaction details and GL system TBs, as well as GL system TBs and the final DDRS-AFS TB used for compiling the DHP's financial statements.

The DHP cannot timely support the current reconciliation process for the financial statement balances. The DHP was unable to produce the UoT reconciliations over FY 2018 Q4 through FY 2019 Q4 to coincide with the delivery of final financial statements. Delivery of completed reconciliations ranged from seven weeks after quarter-close to 12 weeks after quarter-close.

The DHP's Standard Accounting and Reporting System (STARS) – Field Level (FL) GL system is not Federal Financial Management Improvement Act of 1996 (FFMIA)-compliant. Testing identified that STARS-FL does not utilize general ledger account codes (GLAC) which meet the standard GL accounting requirements the Department of the Treasury (Treasury) published in the

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United States Standard General Ledger (USSGL) supplement to the Treasury Financial Manual (TFM). STARS-FL requires the application of complex crosswalks to translate balances from source GLACs to USSGL.

The DHP components did not have sufficient understanding of UoT data produced from ADVANA to timely support critical audit requests during the FY 2019 financial statement audit. Population parameters for significant accounting transaction classes were not readily available and defined with established reporting queries. DHP components were unable to timely provide the population parameters. The nature of the DHP's GL system environment required highly complex population parameters, with voluminous syntax, requiring significant data expertise to reperform the population parameter instructions to reconcile the ADVANA populations. There was incomplete or inconsistent parameter documentation and inconsistent population parameters between component entities utilizing common GL systems. Management needed multiple iterative reconciliation efforts to validate population integrity and population parameters, as well as to perform related analyses.

Cause: The DHP did not maintain effective controls to ensure the UoT reconciliation process was complete and that all identified variances were supported. Material variances were noted as a result of UoT data not containing transactions prior to FY 2013 and variances were noted which remained under research for which no explanation could be provided. In addition, the DHP did not maintain service-level agreements (SLA) or Memoranda of Understanding (MOU) with its service organizations to establish official submission deadlines for key components of the reconciliation process performed each quarter.

The DHP's use of seven GL systems adds complexity, risk, and time to the overall reconciliation process. GL transaction-level data must be obtained, normalized, and reconciled before it is useable across each of the GL systems. Subsequently, the DHP is performing review and approval procedures for each reconciliation package of the seven GL systems. The end-to-end process cannot currently be performed in the compressed financial reporting timeline following quarter-end.

The STARS-FL chart of accounts (COA) does not mirror USSGL account numbers and requires a crosswalk process prior to reporting balances to DDRS-B. STARS-FL is not currently configured to contain all necessary USSGL accounts and attributes when recording transactions.

The processes to utilize ADVANA data to obtain populations for significant accounting transaction classes remained in its infancy during FY 2019, with the DHP Enterprise and components continuing to refine their understanding of the platform. The OUSD(C) and the DHP began training efforts during FY 2019; however, the components were unable to effectively utilize ADVANA for data population analysis. Additionally, the components experienced difficulty in using the system to retrieve large data sets.

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Effect: The DHP is unable to prepare financial statements reconciled to supporting transaction-level data in a timely manner. DHP management is unable to assert to the completeness and accuracy of the financial statements in accordance with GAAP and USSGL Treasury reporting requirements.

The DHP components cannot timely support financial statement population reconciliations. Further, the lack of timely and fully refined population parameters inhibits the DHP's ability to strengthen monitoring activities over financial reporting.

Recommendation: Kearney recommends that the DHP, in coordination with its service organization:

1. Design UoT reconciliation processes to complete tie-out of the GL data to the DHP Enterprise consolidated TB and consolidated financial statements prior to issuance of final financial statements.
2. Complete formalized end-to-end reconciliation process policy or Standard Operating Procedures (SOP) documenting the roles and responsibilities of each stakeholder with established timelines.
3. Develop formal SLAs and/or MOUs to establish a formal delivery timeline of the GL detail, TB detail, journal voucher (JV) detail, and applicable reconciliation packages to the DHP subsequent to each quarter-end.
4. Monitor service organization progress in generating key components of the reconciliation process to allow for alternative procedures if extended delays are anticipated.
5. Continue ongoing efforts to develop and improve the SOP documenting the UoT reconciliation process, to include:
   a. Requesting and receiving data from system/data owners.
   b. Performing reconciliations and reviews of service organization reconciliations.
   c. Documenting change management procedures.
   d. Documenting reviewer responsibilities.
   e. Documenting and researching root causes of variances identified throughout the UoT reconciliation steps, as well as determining the financial statement line item impact of those variances.
6. Continue performing an annual analysis of the financial statement impact of not having GL transaction data to fully reconcile to GL system TBs. Additionally, the DHP should continue to work with the ADVANA service organization to obtain GL transaction data for no-year appropriation funds.
7. Coordinate with the service organization ADVANA Team to continue efforts to resolve variances under research.
8. Implement procedures to complete and document crosswalk reconciliations from GL system TBs to DDRS-B to ensure completeness and accuracy from native GLACs to USSGL. The crosswalk reconciliations should be formalized to allow an external auditor to re-perform the crosswalking exercise from GL system TBs to DDRS-B and from DDRS-B to GL system TBs. Additionally, the DHP should document a process for modifying and/or updating the crosswalks based on changes implemented with the GL

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systems to ensure crosswalks stay current and are reflective of current GL system GLACs.

9. Complete a formalized validation of all data fields from component GL systems which are necessary for inclusion in ADVANA for assessable unit identification, key supporting documentation retrieval, and other reporting requirements as determined necessary. The validation of data fields should include necessary fields which may be required by service organizations for sample support retrieval.
10. Complete a drilldown from the component financial statement line items to significant transaction classes or assessable units to enable population reconciliation from ADVANA GL system data to the component DDRS-AFS TBs and financial statements.
11. Define query parameters using ADVANA data for population reconciliations of significant transaction classes or assessable units. Query design should enable population reconciliation from ADVANA to component GL system TBs.
12. Review and update all population parameters between component entities for common systems to ensure consistency and completeness of sample populations.
13. Update population parameters using a rules-based approach, leveraging field and character identifiers that can be applied across a transaction universe.
14. Review and update the waterfall sequence of population assessable unit parameters to ensure consistency with documentation provided to external stakeholders.
15. Define business rules to identify cost accounting transactions, net to zero transactional activity and other transactions included in ADVANA GL system data which do not have a financial reporting impact. Such transactions should be defined and identifiable when running population queries so such activity can be removed prior to sample selection.

III. Financial Reporting – Defense Departmental Reporting System Adjustments (*Repeat Condition*)

Background: The DHP's service organization for financial reporting posts monthly JV adjustments in DDRS-B and quarterly JV adjustments and trial balance input adjustments (TBIA) in DDRS-AFS on behalf of the DHP components. The financial reporting service organization self-classifies each DDRS-AFS and DDRS-B JV as either "supported" or "unsupported". Monthly, the DHP service organization also prepares, preprocesses, and records various feeder adjustments within DDRS-B. The DHP, in coordination with its service organization, is responsible for ensuring all adjustments to its financial records contain adequate support and approvals.

The DDRS-B module is utilized for budget execution reporting and the DDRS-AFS module combines component TBs into the DHP TB for financial statement reporting. The DHP's service organization reviews the financial statements and footnotes as a part of financial statement compilation and reporting procedures and DDRS-AFS contains automated reconciliations and edit checks.

Included in the monthly and quarterly financial reporting processes are the posting of trading partner adjustments and elimination entries. There are two types of eliminations: 1) intra-DHP eliminations, which are those within the DHP and its components, and 2) inter-DHP

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eliminations, which are those outside of the DHP. Prior to execution of the elimination entries, trading partner seller-side adjustments are made. According to the DoD Financial Management Regulation (FMR), DoD's accounting and feeder systems do not capture trading partner information at the level required to facilitate intra-departmental trading partner reconciliations and subsequent eliminations. Therefore, the buyer-side balances are aligned with seller-side balances, as it is presumed that the amounts reported by the seller are more accurate than corresponding amounts reported by the buyer.

Condition: The DHP's financial statements contain material unsupported JV adjustments. During FY 2019, unsupported adjustments, as self-classified by the DHP's service organization, were posted on behalf of the DHP components in Quarter (Q) 1 and Q2. Of approximately 1,950 JVs recorded as of March 31, 2019, 28% were classified as unsupported. This amounted to an excess of 500 unsupported DDRS-B JVs and 42 unsupported DDRS-AFS and TBIAs.

The DHP, in coordination with its service organization, has not performed an assessment of the known unsupported JVs recorded to determine the impact of unsupported amounts reflected in the DHP financial statements.

The DHP's service organization recorded JVs, self-classified as "supported," which did not contain sufficient supporting documentation. Nineteen JVs impacting the FY 2019 Q2 financial statement balances were noted as exceptions.

The DHP components could not sufficiently support the review and approval of DDRS-B JVs manually recorded by the DHP service organization. Twenty-five JVs were noted as exceptions. JV packages were found to reference expired or non-existent MOUs between the DHP components and the service organization. One additional exception was identified due to a lack of evidence that the DHP component approver held the appropriate level of authority based on the JV dollar amount.

The DHP, in coordination with its service organization, has not ensured feeder adjustments recorded during the monthly DDRS-B reporting process are fully supported by underlying transaction-level data, and it has not fully completed reconciliations from underlying source data to the DDRS-B TB adjustments. The DHP, in coordination with its service organization, has not completed an assessment to collectively determine the financial statement impact of the unsupported feeder adjustments recorded during DDRS-B reporting.

During Q3, the DHP, in coordination with its service organization, reported variances of $1.3 billion between the Standard Form (SF)-133, *Report on the Budget Execution and Budgetary Resources*, and the final Q3 FY 2019 Statement of Budgetary Resources (SBR). The variances were detected within the DDRS-AFS automated reconciliations during the financial reporting compilation but were not corrected prior to issuing final financial statements.

Trading partner seller-side adjustment JVs, recorded in DDRS-AFS to adjust the buyer-side intra-governmental transactions to the seller-side intra-governmental transactions, are unsupported, as no underlying reconciliation of trading partner activity is performed to support

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the adjustments. DDRS elimination JVs (intra-DHP eliminations and inter-DHP eliminations) and reports at the DHP financial statement level lack evidence of review and approval.

Cause: The DHP financial reporting environment is complex, necessitating an inordinate volume of JVs and adjustments to prepare financial statements. The DHP components do not share a common GL system, and each component utilizes a multitude of contributing feeder information systems. Many of these feeder systems and adjustments do not interface with DHP GL systems, but rather underlying activity is recorded directly into DDRS-B and DDRS-AFS via adjustment entries.

The DHP does not exercise oversight of its components and its service organization to enforce the generation and retention of supporting documentation to maintain an audit trail to transaction-level data. The DHP and its service organization have not developed business processes to ensure accounting events are fully supported by adequate underlying documentation. Additionally, the DHP has not documented and exercised sufficient oversight of its DDRS-B feeder adjustments.

The DHP's service organization did not take appropriate remediation action to correct the material error detected by automated DDRS reconciliations performed at the time of Q3 financial statement compilation prior to issuing the final financial statements. The DHP, in coordination with its service organization, did not have timely monitoring of the controls in place to identify, research, and remediate the material misstatement within the DHP SBR prior to finalization of the Q3 FY 2019 financial statements.

The DHP has not established policies or procedures to reconcile intra-departmental transactions and balances with its trading partners. The DHP has not implemented appropriate or effective oversight of its service organization and has not adequately designed or implemented controls for appropriate review and approval over intra-DHP and inter-DHP trading partner eliminations for the DHP's financial statements.

Effect: As a result of the magnitude of unsupported JVs and other adjustments recorded during financial statement preparation, the DHP could not attest to the accuracy and completeness of its FY 2019 opening balances and the financial statement balances impacted by such adjustments recorded during FY 2019. Misstatements to the DHP consolidated financial statements may not be detected and correctly timely, and the DHP is unable to provide audit trails from its detailed feeder adjustment transactions to its financial statements. The volume of unsupported JVs is also an indicator of FFMIA noncompliance as it pertains to recording financial events in accordance with the requirements of the USSGL at the transaction level.

Recommendations: Kearney recommends that the DHP, in coordination with its service organization:

1. Analyze the unsupported DDRS-AFS JVs, DDRS-AFS TBIAs, and DDRS-B JVs to determine the nature of the adjustments. Results of this analysis should be used to identify the nature of the missing underlying support related to the unsupported

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adjustments. Upon completion of the analysis, a Corrective Action Plan (CAP) should be developed by JV category to set a path forward to resolve the underlying reason for the JV.

2. Assess the unsupported JVs to determine the financial reporting impact to the DHP financial statements. The assessment should include appropriate detail to provide the percentage of significant financial statement line items which cannot be asserted for completeness and accuracy as a result of unsupported JVs included in the line item balance.
3. Update existing JV preparation and review procedures to ensure JV packages for supported JVs are complete and include all necessary underlying detail needed to substantiate the supported nature of the adjustment.
4. Coordinate with the DHP components and GL system owners to migrate monthly and quarterly adjustments, such as collections and disbursements, budget, and accountable property system of record (APSR) adjustments, to the DHP component GL systems which can accommodate USSGL reporting and transaction-level details.
5. Update or implement appropriate policies and procedures to facilitate coordination and communication between the DHP components and its service organization to obtain, maintain, and reconcile the underlying transaction-level data necessary to determine and support the monthly and quarterly adjustments for each DHP component and GL system to be entered at the DDRS-B and DDRS-AFS level. The DHP should also continue its efforts to develop and improve documented procedures over the DDRS-B adjustments reconciliation process, to include:
   a. Requesting and receiving data from system/data owners.
   b. Documenting change management procedures.
   c. Documenting reviewer responsibilities.
   d. Documenting and researching root causes of material variances identified throughout the DDRS feeder adjustment reconciliation steps.
6. Complete an analysis to determine the financial statement line item impact of unsupported and unreconciled DDRS-B feeder adjustment balances.
7. Continue to work to obtain detailed transaction-level data for all DDRS-B feeder adjustments, as necessary.
8. Continue efforts to implement reconciliations to support all summarized DDRS adjustment balances with transaction-level detail for all DDRS adjustment files to ensure the completeness and accuracy of the balances reported in DDRS-B.
9. Perform an analysis of the unsupported adjustments to:
   a. Determine the feasibility of obtaining support for these balances.
   b. Determine their financial statement impact.
   c. Determine when the adjustments will cease to impact the DHP financial statements.
10. Formalize and document oversight of all DDRS-B feeder file JVs.
11. Identify, research, and remediate DDRS-AFS reconciliations with material variances, or process necessary adjustments, prior to finalizing quarterly financial statements.
12. Review DDRS reconciliation results prior to financial statements being finalized and communicate material variances within the DDRS reconciliation suite to a sufficient level of DHP management for oversight of accounting operations.

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13. Implement policies and procedures for reconciling trading partner data at the transaction level based on the transactions and source documentation provided by trading partners. Once reconciliations are complete, the DHP should coordinate with its trading partners to adjust balances, as necessary, to reflect the actual amounts incurred and owed to trading partners based on the provision of goods and/or the receipt of services.
14. Update relevant intra-DHP elimination policies and procedures to require its service organization to submit the intra-DHP eliminations with all appropriate and necessary JV support to allow for proper review to be performed by the DHP and to require the coordination directly with trading partners to develop processes for obtaining transaction details for intra-DHP eliminations.
15. Establish an SLA, as may be necessary, to ensure the trading partner elimination notifications occur within business hours, ensuring the DHP's availability for review and approval during the agreed-upon response window within the SLA.
16. Implement formal policies and procedures to perform and document the review of the intra-DHP and inter-DHP trading partner eliminations made on behalf of the DHP. This should include the development of an SOP to ensure that the review and approval process is consistently applied at the Enterprise level.

IV. Fund Balance with Treasury (*Repeat Condition*)

Background: The FBWT account represents the aggregate amount of funds available at Treasury for which DHP components are authorized to make outlays and includes balances held by the entity on behalf of the Government or other entities (which includes clearing/suspense and deposit accounts). FBWT is increased by receiving appropriations, continuing resolutions, transfers-in, and offsetting collections, and it is decreased through rescissions and cancellations of budget authority, transfers-out, and disbursements.

All Treasury Index (TI) 97 Other Defense Organizations (ODO), including DHP components, are assigned specific Treasury Account Symbols (TAS) and limits. Limits designate the amount or use of funds for a certain purpose or identify sub-elements within the account for management purposes. Federal agencies are required to reconcile FBWT at the TAS level. In addition, DoD requires TI 97 ODO components to reconcile below the TAS to the limit level. Reconciling FBWT accounts with Treasury's Central Accounting Reporting System (CARS) records at least monthly helps ensure that balances are accurate and complete, differences are resolved in a timely manner, and financial statements are presented fairly. The DHP utilizes a service organization to perform monthly reconciliations between recorded amounts and those reported to Treasury at the TAS and limit level.

In addition to supporting FBWT reconciliations, the service organization processes collections and disbursements and reports the DHP's total expenditure activity to Treasury on behalf of the Enterprise. Statements of Differences (SOD) arise when amounts reported to Treasury differ from actual disbursements and collections processed by financial institutions and the Treasury Regional Financial Centers. When reported transactions cannot be linked to a specific appropriation or reporting entity, they are placed into a DoD budget clearing (suspense) account for research and resolution.

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Condition: The DHP experienced the following issues regarding the accuracy and completeness of collections and disbursements and related changes to FBWT:

- The DHP, in coordination with its service organization, does not have a complete, documented, end-to-end reconciliation process over FBWT
- The DHP does not have controls over the monitoring of its service organization FBWT processes, including the review, approval, and monitoring of monthly FBWT reconciliations and variance resolution to ensure FBWT is accurate and complete
- The DHP's financial statements include an unsupported/unreconciled opening FBWT balance of $868.6 million, or 4.23% of the DHP's opening FBWT balance
- The DHP, in coordination with its service organization, has not implemented internal control activities to help ensure the accuracy and completeness of the DHP's financial statements with respect to identifying and properly recording actual or estimated suspense and SOD balances
- The DHP's service organization FBWT reporting and reconciliation controls were not operating effectively and the DHP does not monitor or review its service organization processes to ensure FBWT is accurate and complete
- Cash Management Report (CMR) reconciliations, which are used to reconcile CARS TASs to TI-97 ODO TASs and limit balances, are not properly designed. The DHP, in coordination with its service organization, does not research and resolve reconciling and unidentified differences timely and could not produce the underlying support for the unallocated funding balances which impact DHP basic symbols
- A monthly reconciliation is not performed between the CMR and DHP components' TBs at the limit level after all adjustments are recorded
- The DHP, in coordination with its service organization, does not have an effective process to support monthly undistributed adjustments recorded during the financial statement compilation process and not all undistributed reconciling items and unidentified differences are included in the DHP financial statements.

Cause: The DHP, in coordination with its service organization, has not designed all necessary internal control activities or documented its end-to-end FBWT reporting and reconciliation process and associated risks. To further complicate the process, Treasury does not report FBWT at the limit level below the TAS, inhibiting DHP components' abilities to reconcile directly with Treasury.

FBWT reporting and reconciliation controls performed on behalf of the DHP are ineffective due to incomplete policies and procedures, ineffective management review and approval, failure to adhere to defined policies for timeliness, and a lack of consistent policy requirements across service organization locations.

The DHP's service organization has not designed and implemented effective controls to reconcile with Treasury, resulting in reconciling and unidentified differences, as well as unsupported unallocated funding amounts. In addition, the service organization has not designed and implemented effective controls to verify the accuracy of the DHP component FBWT

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balances by reconciling and resolving differences between the CMR and DHP component reported amounts, including CMR undistributed disbursement and collection adjustments.

The DHP and its components have not formally developed and implemented oversight procedures or mitigating controls to compensate for the risk of ineffective controls over the FBWT reconciliation process.

Effect: The DHP may not be able to assess the potential risks to the accuracy and completeness of FBWT without a complete end-to-end reconciliation process, and the DHP may be unable to determine the total unsupported differences between its recorded FBWT and the balance reported in CARS. Without aggregating and reconciling component-level FBWT reconciliations, DHP management may also be unaware of a potential risk of a financial statement misstatement.

Recommendations: Kearney recommends that the DHP, in coordination with its service organization:

1. Develop an accounting policy for FBWT which specifically addresses the requirements for a complete end-to-end FBWT reconciliation process to be performed at the component and DHP levels.
2. Identify impediments to the TI-97 FBWT reconciliation process (e.g., excluded activity from the CMR, TI-97 budget clearing and deposit accounts) and develop compensating controls at the DHP and component levels to reconcile any excluded FBWT activity or, through documented materiality analysis, indicate that management accepts the risk of potential misstatement.
3. Perform root cause analysis to assess underlying business processes which are triggering the high volume and dollar amount of undistributed transactions. Corrective actions in core GL systems should be initiated to begin relying on GL system data and transition away from non-GL systems (e.g., Headquarters Accounting and Reporting System [HQARS], Defense Cash Accountability System [DCAS], CMR) in the financial reporting and compilation process.
4. Establish DHP and component oversight procedures over FBWT processes performed, including identifying and documenting roles and responsibilities for FBWT reconciliations, reviewing and approving reconciliations performed, and performing causative research, for reconciling items identified on a monthly basis.
5. Work with Treasury to determine the feasibility of adding subaccounts to basic symbols (e.g., 0130, 0500) to allow the DHP and its components to reconcile directly with Treasury.
6. Work with applicable parties to transition away from using monthly non-Treasury Disbursing Office reporting to daily Treasury Disbursing Office reporting.
7. Develop and implement a methodology to identify the actual or estimated impact of SODs, budget clearing accounts, and deposit accounts for recording and reporting into the GLs and financial statements.
8. Develop, implement, and document an effective reconciliation process for identifying any unmatched disbursements and collections and ensure that all resulting adjustments are fully supported at the DHP component level.

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9. Review unidentified CMR differences and provide supporting information to clear differences.
10. Research and resolve SODs and suspense transactions by correcting the transactions in source systems and assist with necessary supporting documentation for corrections, if needed.

V. Medical Revenue and Associated Receivables (*Repeat Condition*)

Deficiencies in two related areas define this material weakness:

A. Accounting and Reporting of Medical Services Provided
B. Medical Coding Accuracy.

Background: The DHP SMA components process both billable and non-billable medical encounters that arise from performing medical services. Billing consists of the MTFs sending invoices to patients, agencies, or other third parties for medical services provided. Billable encounters are processed for patient care provided to non-TRICARE beneficiaries or for patient care provided to TRICARE beneficiaries who are either uncovered or covered by other insurance. The SMAs utilize a billing and collection system as a subsidiary ledger to track and process collections on medical billings.

SMA MTFs also provide medical services for beneficiaries that are dual-eligible under Medicare, as well as Federal beneficiaries of the United States Coast Guard (USCG), Public Health Service (PHS), National Oceanic and Atmospheric Administration (NOAA), and Department of Veterans Affairs (VA). Payment for services provided to such beneficiaries varies based on established agreements with each entity.

Care for qualified health care recipients and their families begins at the Patient Administration Department (PAD) of MTFs. A PAD Specialist is responsible for entering a patient's information into supporting medical systems and checking eligibility information against the Defense Enrollment Eligibility Reporting System (DEERS). The verification of patient eligibility is important at the time care is delivered, as eligibility may change based on the timing and nature of services being provided, as well as beneficiary circumstances which may impact their eligibility (e.g., third-party insurance, marital status changes). A patient category (PATCAT) code is ultimately assigned, which is subsequently used by MTF business centers in determining coverage and cost of care.

Medical services provided at SMA MTFs are required to be coded within 30 days of the patient's discharge, which initiates the billing process. Medical coding consists of taking the medical services rendered to a patient and entering the applicable codes using the Defense Health Headquarters (DHHQ) distributed coding tables. DHA contracts with a third-party to perform annual audits over the SMA MTFs' medical coding accuracy in accordance with DoD Instruction (DoDI) 6040.42, *Management Standards for Medical Coding of DoD Health Records*. The most recent available third-party audit results are the FY 2018 coding audit, which represents an audit of medical records that were coded in FY 2017. During the audit,

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approximately 2,600 coded encounters were selected for testing, consisting of both billable and non-billable claims, across all SMAs.

A. Accounting and Reporting of Medical Services Provided

Condition: The DHP SMA components do not account for revenue or AR resulting from medical services provided in a consistent manner, and the accounting for such activity is not in accordance with GAAP.

- Not all SMA components record revenue earned from medical services provided to Federal trading partners on an accrual basis; rather, revenue is recorded on a cash basis. SMAs issue bills for medical services but records associated Federal revenue upon cash receipt in each respective GL system. No process is in place to completely correct the cash basis of accounting for Federal services provided for the DHP
- AR associated with medical services provided to Federal trading partner beneficiaries are not always collected in a timely manner
- Not all revenue earned from services provided to the public are recorded on an accrual basis; rather, certain classes of revenue are recorded on a cash basis
- Monthly JVs recorded by the DHP's service organization to record medical services provided to the public contained posting logic errors, failing to recognize revenue
- SMAs do not consistently and accurately present revenue and AR at net realizable value (NRV). SMAs have not established appropriate allowance for uncollectible accounts or alternatively adjusted revenue and AR to reflect NRV, as appropriate (e.g., Federal AR where an allowance for uncollectible accounts is not prescribed by OMB).

The DHP SMA components receive quarterly prospective payments in advance of care provided from two Federal trading partners. The accounting for prospective payments is not consistent across the SMAs. The SMAs either recognize revenue upon receipt of payment prior to performing services, which is not in accordance with GAAP, or recognize the prospective payments as unearned revenue with periodic recognition over time based on actual care provided or historical data. The DHP did not establish a formalized process to timely assess the reasonableness of its revenue recognition methodology to appropriately adjust revenue based on current-year care provided, as may be appropriate for financial reporting purposes.

The DHP SMA components do not have an internal control in operation to sufficiently demonstrate that patient eligibility confirmation is performed by an authorized PAD Specialist, ensuring accurate eligibility information from within DEERS is being used in determining patient PATCAT codes.

The DHP components are not all able to provide sufficient audit evidence to support the validity of AR balances within the billing and collection subsidiary ledger. DHP component remediation efforts remained in process during FY 2019 to correct AR transactions noted as invalid because they were previously collected and never closed in the system and to provide sufficient documentation to support amounts billed for services provided.

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Cause: The DHP has not formulated and implemented complete Enterprise-wide accounting policies or guidance for its components to ensure consistent and accurate accounting of medical services provided in accordance with GAAP.

The DHP has not implemented an effective Enterprise approach for conducting business with all Federal trading partners that allows for consistency across MTF locations and the timely collection of payment for services provided. Additionally, formalized accounting policy and procedures have not been developed to appropriately account for Federal AR and associated revenue at NRV. Claims are often disputed, rejected, or partially paid based on the billing rates for the services provided or not having prior authorization for care provided to non-DoD beneficiaries. Federal trading partners are also not always timely with their resolution of bills received from the DHP.

SMAs have not established effective business processes with associated internal controls to properly recognize medical service revenue and associated AR using the accrual basis of accounting. In addition, specific to Federal prospective payments received for care to be provided, SMAs have not established an effective business process with associated internal controls to properly recognize revenue based on care provided from actual activity occurring in the current FY or based on supporting validation of its prospective payment methodology for year-end reporting.

The DHP has not established effective business processes to properly perform and/or sufficiently demonstrate patient check-in procedures regarding eligibility, as well as billing, collecting, closing, and recording of medical AR in its subsidiary system. The DHP's remediation efforts to develop, maintain, and provide sufficient documentation to adequately support the reported medical AR remains in process.

Effect: The DHP's financial statements may contain misstatements associated with AR and Other Liabilities (as associated with prospective payments) on the balance sheet, as well as Revenue and Expenses on the Statement of Net Cost. In addition, any unrecorded Federal AR would result in the understatement of Spending Authority from offsetting collections presented on the SBR.

Unrecorded AR and the untimely collection of AR also inhibits the efficient and effective use of the DHP's spending authority, as such collections are made available for obligation in the appropriation year collected as authorized by public law.

The lack of Enterprise-wide policies and guidance for the accounting treatment of medical services resulted in inconsistent accounting treatment across the SMAs, as well as noncompliance with Federal accounting standards and, accordingly, the FFMIA.

The lack of formalized internal control activities over patient eligibility verification inhibits the DHP's ability to ensure medical care provided to patients is a specifically covered benefit. The risk of uncovered care provided to beneficiaries, or care provided to ineligible beneficiaries, may be elevated without proper procedures in place to demonstrate the eligibility verification.

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Recommendations: Kearney recommends that the DHP develop an accounting policy for medical services revenue and associated AR, which specifically addresses the appropriate accounting treatment as prescribed within SFFAS No. 1 and SFFAS No. 7. The accounting policy should be developed through coordination with all SMAs. In addition, DHP SMAs should also perform the following:

1. Review and assess the Enterprise approach for doing business with Federal trading partner beneficiaries and implement, as appropriate, baseline requirements to be met at the MTF level.
2. Implement required pre-authorization to administer care to Federal trading partner beneficiary patients and begin monitoring activities for proper implementation.
3. Formalize revenue recognition when services are performed for all Public AR categories. Revenue and corresponding AR should be recognized with transactional activity recorded in the GL system or as appropriate in a subsidiary system.
4. Formalize revenue recognition procedures for Federal trading partners to be aligned with actual care provided in the current FY, as applicable for each SMA. Revenue recognized should be supported by transactional activity recorded in the GL system or in a supporting subsidiary system.
5. Implement a consistent methodology for the calculation of allowance for uncollectible accounts with inclusion of all AR categories in the calculation. Separate allowance methodologies should be considered by AR category based on historical collection analysis.
6. Implement consistent methodology for adjusting gross AR and associated revenue to reflect NRV for receivable categories which the DHP does not deem an allowance to be appropriate (e.g., third-party collections or Federal receivables).
7. Review current procedures related to patient eligibility and incorporate formalized verification procedures which can demonstrate the eligibility determination at the time of patient check-in or at an appropriate point during the patient lifecycle prior to the patient's final paperwork completion.
8. Perform documented reconciliation of medical AR recorded in the subsidiary ledger with medical AR recorded for financial reporting, including supervisory review and approval.
9. Design and implement a process to verify that collected patient billings are appropriately closed in the subsidiary ledgers. Monitoring controls should be established, to include performing a reconciliation between aged AR balances in the subsidiary ledger and collections to ensure that invalid AR entries have been closed.
10. Formalize supporting documentation and retention requirements to demonstrate the validity of patient billings.

B. Medical Coding Accuracy

Condition: The DHP has not implemented effective medical coding procedures to ensure the accuracy of medical coding applied over inpatient (IP), outpatient (OP), ambulatory procedure visit (APV), and inpatient professional service round (IPSR) healthcare encounters. The third-party medical coding audit report released during FY 2019, entitled "Fiscal Year 2018 Military Treatment Facility Coding Audit Findings and Recommendations," identified coding errors

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significantly below the required 97% accuracy threshold prescribed within DoDI 6040.42. Accuracy rates were noted as:

- 30% for OP
- 51% for APV
- 84% for IP
- 27% for IPSR.

Cause: The findings and recommendations included in the FY 2018 medical coding audit indicate that the DHP does not have sufficient clinical supporting documentation that clearly and specifically addresses the procedures performed during patient encounters for accurate medical coding. Additionally, the audit report indicates that the DHP lacks the appropriate ongoing education and training courses to improve the coding staff's expertise to appropriately code the encounters.

Effect: Medical AR billing valuation and the corresponding revenue recorded is determined, in part, by the prescribed medical code being aligned to a corresponding prescribed rate for the coded encounter. Therefore, the DHP cannot assert to the accuracy and valuation of AR recorded for medical billing encounters, and the DHP's recorded Revenue and AR line items may be misstated as presented on the Statement of Net Cost and balance sheet, respectively.

The current design and scope of the third-party audits are not sufficient to ascertain the financial reporting impact of the medical coding inaccuracies. The audit contract with the third-party coding auditor does not require medical coding audits for billable encounters, separate from non-billable encounters. As a result, the DHP cannot ascertain if coding accuracy for billable encounters is sufficient as compared to non-billable encounters.

Recommendations: Kearney recommends that the DHP formally develop and implement the following:

1. Review the third-party audit findings and recommendations and formally develop appropriate CAPs, as necessary, to remediate coding accuracy deficiencies. CAPs should be developed with input from across appropriate stakeholders of the DHP components.
2. Revisit the contract with the third-party coding auditor and incorporate separate auditing efforts over billable medical encounters. This would allow the DHP to assess the financial reporting impact of any coding inaccuracies found during the third-party audits. Coding audits over billable encounters should be designed with an appropriate methodology to extrapolate audit results to the billable encounter population. Appropriate analysis of the error rates should be conducted to determine the impact of error rates over applicable financial statement line items (e.g., AR and Revenue).

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VI. General Equipment Existence and Completeness (*Repeat Condition*)

Background: FASAB defines general equipment (GE) as all personal property that is functionally complete for its intended purpose, durable, and nonexpendable. Additionally, GE typically has an expected service life of two or more years, is not intended for sale, does not ordinarily lose its identity or become a component part of another article when put into use, and has been acquired (or constructed) with the intention of being used .

Condition: The DHP did not record GE in a consistent manner across component reporting entities. One DHP component could not support the opening balance of GE reported for FY 2019 with sufficient documentary evidence, reversing the opening balance to $0 in Q1 of FY 2019. During FY 2019, the component was unable to sufficiently determine the existence, completeness, or valuation of its GE asset portfolio for financial reporting purposes, and no GE was recorded. The component does not have formal policies or procedures documenting its operational processes and controls to identify, track, record, and value its GE in accordance with GAAP, as promulgated by FASAB.

The remaining DHP components, in aggregate, did not demonstrate sufficient existence and completeness for GE which was recorded for FY 2019. The DHP could not locate or did not provide sufficient audit evidence to support the existence of 14% of 331 tested assets. The DHP did not record or did not provide sufficient appropriate evidence to support approximately 8% of 139 tested assets, which were selected while performing testwork at DHP MTF locations (i.e., completeness of DHP recorded assets).

Cause: The DHP has not completely implemented policies, procedures, or internal controls to identify, recognize, and report capital GE for all component entities. The DHP is currently in the process of completing its assessment of capital GE at various locations and, therefore, has not yet finalized its approach to valuing GE.

Existence and completeness exceptions over GE are due to the lack of effective inventory management controls, inaccurate reporting of assets within the APSR, and lack of effective retention of supporting documentation.

Effect: Ineffective inventory management controls may result in the loss of accountability for asset custodianship and unsupportable financial reporting over PP&E. Further, the DHP cannot assert that the PP&E balance is fairly stated in accordance with GAAP. The DHP could not provide sufficient appropriate evidence of the existence and completeness for approximately 12% of tested assets, which may represent potential misstatements to the PP&E balance as of September 30, 2019.

Recommendations: Kearney recommends that the DHP:

1. Establish an Enterprise-wide accounting policy to require annual inventory of GE, tracking GE, and proper cost classification in accordance with SFFAS No. 6, to include appropriate footnote disclosures.

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2. Develop financial reporting policies and procedures to ensure that the DHP's operational business processes are reviewed to determine the appropriate accounting treatment, recording, and financial reporting impact.
3. Complete ongoing efforts to verify the existence and completeness of GE for the purpose of bringing the GE portfolio to record for financial reporting.
4. Perform a final assessment of available supporting documentation based on the known exceptions from testwork. Adjustments to the component APSRs should be recorded to remove known existence exceptions and add any remaining known completeness exceptions from the asset detail schedule.
5. Disseminate the GE existence and completeness audit testing results to all equipment custodians to promote awareness of the impact that effective inventory management controls have on property accountability.
6. Adhere to criteria and internal guidance related to the proper storing of documentation to support the acquisition, transfer, and disposal of GE.

VII. Valuation of Property, Plant, and Equipment (*Repeat Condition*)

Background: DHP components own, operate, and maintain stewardship of a diverse and significant portfolio of PP&E. The DHP has determined the asset classes for its PP&E as follows: GE; Real Property construction in-progress (CIP); internal use software (IUS); IUS in-development; heritage assets; leases; and leasehold improvements. The DHP reported PP&E, net of accumulated depreciation and accumulated amortization, to be $3.2 billion.

In August 2016, FASAB issued SFFAS No. 50, *Establishing Opening Balances for General Property, Plant, and Equipment*, amending existing PP&E accounting standards to allow a reporting entity, under specific conditions, to apply alternative valuation methods in establishing opening balances for PP&E. The alternative valuation methods available under SFFAS No. 50 may be applied in the first reporting period in which the reporting entity makes an unreserved assertion that its financial statements are presented fairly in accordance with GAAP. As SFFAS No. 50 is applicable to the valuation of opening balances only, all changes to the DHP PP&E portfolio as a result of current-year transactions are subject to the valuation requirements set forth in SFFAS No. 6.

Condition: The DHP PP&E valuation as of September 30, 2019 is not in accordance with GAAP. The PP&E balances have not been valued at historical cost in accordance with valuation techniques promulgated by SFFAS No. 6. Further, the DHP did not begin valuation efforts over PP&E using alternative valuation techniques (i.e., deemed cost) in accordance with SFFAS No. 50.

Cause: The DHP has not established effective business processes, internal controls, or information systems necessary to accurately value PP&E in accordance with SFFAS No. 6. The accumulation of historical cost information with supporting documentation for PP&E acquisitions has not been appropriately maintained to support acquisition costs recorded in property systems. While the DHP intends to elect the alternative valuation techniques within SFFAS No. 50 to report property balances, it was not ready to make the election within FY 2019.

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The DHP formulated draft accounting guidance for the GE asset class during FY 2019; however, the guidance was not finalized by September 30, 2019. The draft guidance does not specifically address valuation for opening balances under SFFAS No. 50.

Effect: The DHP is unable to accurately and appropriately value its PP&E assets for FY 2019 in accordance with GAAP. The lack of accounting policy from an Enterprise perspective has resulted in a lack of preparedness at the component level to re-value FY 2019 PP&E opening balances at historical cost in accordance with SFFAS No. 50.

The DHP's PP&E as of September 30, 2019 does not reflect historical cost as required by SFFAS No. 6, and the DHP's opening balances for FY 2019 do not reflect historical cost under alternative valuation techniques as allowable under SFFAS No. 50. The DHP's recorded balance for PP&E, net of accumulated depreciation and accumulated amortization, of $3.2 billion may be materially misstated as presented within the DHP's financial statements.

Recommendations: Kearney recommends that the DHP:

1. Develop an Enterprise-wide accounting policy for PP&E, which specifically addresses historical cost valuation in accordance with SFFAS No. 6 and SFFAS No. 50. In its determination to implement historical cost valuation for opening balances under SFFAS No. 50, the DHP must implement PP&E processes with supporting internal controls that are both designed and operating effectively to value new PP&E acquisitions at historical cost in compliance with SFFAS No. 6.
2. Reference FASAB's Federal Financial Accounting Technical Release (TR) No. 18, *Implementation Guidance for Establishing Opening Balances*, dated October 2, 2017.
3. Retain appropriate key supporting documentation for underlying valuation methodology.
4. Document the valuation technique by asset class for all assets currently in the DHP PP&E portfolio.
5. Establish a timeline for the valuation and steps that each component is required to perform.
6. Detail requirements for valuation of new acquisitions that are compliant with SFFAS No. 6.

VIII. Real Property (*Repeat Condition*)

Background: DHP components own, operate, and maintain stewardship of a diverse and significant portfolio of PP&E Real Property (hereafter referred to as real property). Health care provided by the DHP is delivered in MTFs, which constitute more than 51 full-service hospitals and over 424 clinics located on military installations around the world.

SMA components' construction agents (i.e., Naval Facilities Engineering Command [NAVFAC] and United States Army Corps of Engineers [USACE]) oversee routine maintenance and major repairs for the various DHP real property assets. The DHP's real property capitalization threshold is $250 thousand for each component. For all components, construction projects may be funded using Operations and Maintenance (O&M) funds for projects under $1 million and are

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funded with Military Construction (MILCON) funding if above $1 million. Regardless of funding type, capital improvements should be capitalized as CIP for accurate financial reporting.

Condition: The DHP Enterprise has not complied with SFFAS No. 6, *Accounting for Property, Plant, and Equipment*, in the accounting treatment and financial reporting of real property. The DHP did not record real property as part of the PP&E opening balance as of October 1, 2018, and real property was not subsequently added during interim reporting periods as of March 31, 2019, June 30, 2019, or year-end reporting as of September 30, 2019.

SMA components do not have a process in place to record real property CIP related to O&M-funded projects for financial reporting. The SMA components do not assess and monitor O&M projects to determine if the project meets the requirements for capitalization, nor do they track and accumulate costs for capitalization from O&M-funded projects.

Cause: The decision to withhold real property from the DHP's financial statements was based on the revisions to DoD-wide accounting policy related to the financial reporting responsibilities of real property. The accounting policy changes became effective October 1, 2019; as a result, the DHP did not prioritize remediation efforts of real property financial reporting. The DHP did not develop an accounting policy or standard guidance for component reporting entities to value and record real property.

SMA components have not applied their capitalization policies to real property CIP projects funded by O&M appropriations. Additionally, SMAs have not established effective internal controls to track and record capital costs related to O&M-funded CIP.

Effect: The DHP has not complied with SFFAS No. 6 in the accounting treatment and financial reporting of real property. General PP&E, as presented on the balance sheet, is understated by the omission of the DHP's real property. Any corresponding depreciation expense is understated on the Statement of Net Cost. The DHP cannot quantify the potential understatement to PP&E on its financial statements.

Without a process in place to track and record capital costs related to real property CIP funded by O&M appropriations, there is an overstatement of gross costs and understatement of PP&E, net balances within the DHP's Statements of Net Cost and balance sheet, respectively.

Recommendations: Kearney recommends that the DHP:

1. Conduct an existence and completeness review of all real property (e.g., facilities, linear structures) associated with the DHP's health support for all military operations. Working with the Navy, Army, and AF, the DHP should determine which reporting entity meets the FASAB requirements for ownership and recognition of real property.
2. Incorporate real property in the development of Enterprise accounting policy for PP&E, aligning, as appropriate, with the financial reporting responsibilities of real property prescribed at the DoD-wide level.

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3. Assess the impact of new DoD-wide policy for real property financial reporting responsibilities as applicable to the DHP in FY 2020 and beyond. In accordance with the new policy, the DHP is required to:
   a. Maintain a list of all real property facilities the DHP occupies and for which it has facility operations and maintenance or facility improvement responsibilities.
   b. Record key data elements for financial reporting as prescribed.
   c. Establish MOAs with each installation host, defining the rights and obligations between the installation host and the DoD component using the real property asset. An MOA must identify the roles and responsibilities of the host and tenant, as well as detail the respective maintenance and other operational responsibilities between the host and tenant.
4. Coordinate with constructions agents (i.e., NAVFAC and USACE), as appropriate, to develop and implement policies and procedures that track and account for capitalized costs related to O&M-funded CIP. The policy and procedures should include a formalized assessment of construction projects prior to project commencement to determine if criteria for capitalization has been met. O&M projects should be indicated as capital vs. non-capital within the relevant APSR based on the documented assessment.
5. Provide training to DHP personnel to ensure policies and procedures to track and record O&M-funded CIP are implemented accordingly.
6. Implement internal controls over financial reporting to verify that all capital renovation and improvement projects that meet the DHP's capitalization thresholds are captured for financial reporting purposes on the balance sheet. The DHP should formalize a data call at the region level on a quarterly basis to monitor appropriate capitalization decisions for O&M-funded projects.

IX. Internal Use Software and Internal Use Software In-Development (*Repeat Condition*)

Background: IUS includes application and operating system programs, procedures, rules, and any associated documentation pertaining to the operation of a computer system or program that an entity uses in operations or for other internal use. IUS does not include software embedded in military equipment, nor does it include software used in Special Test Equipment. IUS may be acquired through commercial off-the-shelf (COTS) purchases, developed by entity employees, or developed by contractors to the entity.

IUS owned by the DHP includes the Armed Forces Billing and Collection Utilization Solution (ABACUS), Composite Health Care System (CHCS), and Defense Medical Logistics Standard Support (DMLSS). In July 2015, an Indefinite Delivery, Indefinite Quantity (IDIQ) contract was awarded with a ceiling value of $4.3 billion to provide an electronic health record (EHR) solution for the MHS. This contract was funded by the DHP using Research, Development, Test, and Evaluation (RDT&E) funds. The MHS's EHR system, MHS GENESIS, will collect, process, and provide health records to the DoD beneficiaries and is managed under the Program Executive Office (PEO), Defense Healthcare Management System (DHMS).

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As previously detailed in Section VII, *Valuation of Property, Plant, and Equipment*, DHP management did not make an unreserved assertion as it pertains to the implementation of SFFAS No. 50. Without an unreserved assertion for SFFAS No. 50, the governing FASAB standard for the DHP's IUS is SFFAS No. 10.

Condition: The DHP's FY 2019 valuation of IUS, including IUS in-development, is not in accordance with GAAP. The DHP did not record IUS as part of opening balances of PP&E for FY 2019. The DHP did not begin valuation efforts over IUS using alternative valuation techniques in accordance with SFFAS No. 50, and it is unable to value IUS at historical cost in accordance with SFFAS No. 10.

The DHP does not have a formal process in place to track, classify, and accumulate the costs of the MHS GENESIS in order to identify and support proper accounting classification and financial reporting requirements. As of September 30, 2019, MHS GENESIS has not been recorded on the DHP's balance sheet as a capital asset. MHS GENESIS has launched at multiple sites, with full deployment scheduled to be completed in FY 2024. As of May 2019, the DHP reported $1 billion in obligations related to the MHS GENESIS and $916.7 million in expenditures.

Cause: With the DHP's intent to implement SFFAS No. 50 for IUS valuation, there has been an historical lack of effective business processes, internal controls, and information systems in place to accurately account for IUS in accordance with SFFAS No. 10. The DHP has not implemented policies, procedures, or internal controls to inventory IUS currently in use, track IUS projects in-development, and determine appropriate cost classification of expenditures for proper financial reporting.

The DHP has not finalized its approach to valuing IUS and IUS in-development in accordance with SFFAS No. 50 for opening balances and SFFAS No. 10 on a go forward basis after opening balances have been asserted to by management.

The DHP has not performed a complete assessment of operational business processes to determine the financial reporting impact and proper accounting treatment of operations.

The DHA component and PEO DHMS have not adequately communicated regarding the MHS GENESIS development phases and schedule in order to support a decision regarding the accounting classification and financial reporting of the MHS GENESIS procurement as IUS or IUS in-development.

Effect: The DHP is unable to accurately account for the existence, completeness, or valuation of IUS and IUS in-development, and the DHP has not complied with the accounting and financial reporting requirements of SFFAS No. 10. General PP&E, as presented on the balance sheet, is understated by the omission of the DHP's IUS and IUS in-development, which includes MHS GENESIS. Period expenses are overstated by any cost related to the development of IUS occurring in FY 2019, including any capital costs associated with the development and implementation of MHS GENESIS.

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Due to the lack of controls surrounding IUS in-development and tracking, sufficient audit evidence was not provided to quantify the misstatement and, therefore, conclude whether the DHP's PP&E is fairly stated in accordance with GAAP.

Recommendations: Kearney recommends that the DHP:

1. Develop and implement an accounting policy for IUS. The policy should provide for annual inventory of IUS, tracking IUS in-development, proper cost classification, and proper valuation in accordance with SFFAS No. 50 and SFFAS No. 10.
2. Continue pursuing expanded functionality in the IUS APSR to track and inventory IUS and IUS in-development to support the completeness and valuation of the IUS balance.
3. Develop annual inventory and accountability procedures in compliance with the DoD FMR and DoDI 5000.76, *Accountability and Management of Internal Use Software*.
4. Design and implement formalized internal controls for proper cost classification associated with IUS in-development to facilitate the identification and reporting of capital costs.
5. Develop a valuation strategy and approach for the financial reporting recognition of MHS GENESIS.
6. Develop a working group with DHA and PEO DHMS to foster appropriate information-sharing to classify and report MHS GENESIS for financial reporting purposes. The working group should consider developing items such as:
   a. A complete inventory of contracts that have been procured to support the implementation/integration of MHS GENESIS at MTFs.
   b. Designated POCs from DHA and PEO DHMS with the responsibility of reviewing monthly MHS GENESIS expenditures and making decisions regarding the proper expenditure classifications.
   c. An understanding of the invoice process to determine how costs are accumulated and reported within the GL system(s), as well as a decision regarding how to track all costs.
   d. An understanding of any enhancements and their impact to DHA's accounting treatment and financial reporting of MHS GENESIS.
   e. A decision regarding how the MHS GENESIS will be defined, classified, and reported on the financial statements.
   f. Procedures regarding how DHA will bring MHS GENESIS to record for financial reporting purposes.
   g. Supporting documentation requirements to identify what is available or will be available to support DHA's decisions and conclusions regarding the accounting treatment, classification, and financial reporting of MHS GENESIS.
7. Design and implement formalized internal controls for proper cost classification associated with MHS GENESIS to facilitate the identification and reporting of capitalizable costs.

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X. Operating Material and Supplies and Stockpile Material (*Repeat Condition*)

Deficiencies in two related areas define this material weakness:

A. Enterprise Assessment of Operating Material and Supplies
B. Policies, Procedures, and Controls Surrounding Stockpile Materials Held by the Defense Health Program.

Background: SFFAS No. 3 defines operating materials and supplies (OM&S) as tangible personal property to be consumed in normal operations with the exclusion of: 1) goods that have been acquired for use in constructing real property or in assembling equipment to be used by the entity; 2) stockpile materials; 3) goods held under price stabilization programs; 4) foreclosed property; 5) seized and forfeited property; and 6) inventory. Per SFFAS No. 3, the consumption method of accounting must be applied unless it is: 1) not significant amounts; 2) in the hands of the end user; or 3) if it is not cost-beneficial to apply the consumption method, the purchases method may be applied. DHP components' OM&S encompasses pharmaceuticals, pharmaceutical medical supplies, and non-pharmaceutical medical supplies needed for MTFs.

DHP components are also required to maintain various medications for the DoD to respond to a pandemic or other public health emergency. The DHA component maintains SLAs with Federal entities to purchase medications on behalf of DHA. DHA also maintains SLAs to store and distribute medication materials for medical preparedness. Medications purchased for DHA by other Federal entities remain at the manufacturing facility until such time that they need to be administered throughout the DoD.

A. Enterprise Assessment of OM&S

Condition: The DHP has not performed an annual assessment of OM&S for the purposes of determining appropriate accounting treatment under SFFAS No. 3. Currently, OM&S acquired has been directly expensed as allowable under SFFAS No. 3; however, the DHP has not conducted a formalized annual assessment of its OM&S portfolio to determine whether directly expensing acquisitions is appropriate. The DHP has not documented its determination of whether OM&S are significant amounts, in the hands of the end user for use in normal operations, or if it is cost-beneficial to capitalize OM&S.

Cause: The DHP has not developed and implemented policies and procedures to ensure that OM&S acquired by component reporting entities are appropriately and accurately accounted for and captured in the DHP's financial statements in accordance with Federal accounting standards.

Effect: The opening balance of Inventory and Related Property, as required to be reported on the DHP Enterprise balance sheet and disclosed in the supporting footnotes, may be incomplete and the corresponding expenditures associated with the purchase and issuance of OM&S may be misstated on the Statement of Net Cost.

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As a result of the DHP's lack of formalized assessment of OM&S, the DHP could not demonstrate the fair presentation of Inventory and Related Property in accordance with GAAP.

Recommendations: Kearney recommends that the DHP:

1. Develop and implement a strategy to perform an annual assessment to support the elected accounting treatment for OM&S under SFFAS No. 3.
2. Support the assessment with formalized documentation, demonstrating the selected criteria and applicable analysis.

If the DHP is unable to support one of the three criteria required for directly expensing OM&S acquisitions, Kearney recommends that the DHP:

1. Develop and implement a strategy to verify the existence, rights and obligations, valuation, and completeness of OM&S at the DHP and component levels.
2. Evaluate flexibilities provided by SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials*, to establish opening balances.
3. Develop a DHP strategy for valuing, recording, maintaining (accountability), and reporting OM&S to provide guidance to the components.
4. Develop an Enterprise-wide policy to define the appropriate accounting treatment, recording, and financial reporting of OM&S.

B. Policies, Procedures, and Controls Surrounding Stockpile Materials Held by the DHP

Condition: The DHP components did not account for stockpile material in accordance with requirements set forth in SFFAS No. 3. Throughout FY 2019, the DHP incorrectly expensed stockpile material upon purchase, rather than appropriately capitalizing the stockpile material on the balance sheet. In Q4 of FY 2019, one DHP component recorded an adjustment of approximately $52.1 million of stockpile materials as of September 30, 2019. The adjustment reflects the remediation efforts of a new data call process implemented by one DHP component to obtain stockpile material data from MTF locations for the purpose of financial reporting requirements. The DHP component remediation efforts to validate the new process and test the existence and completeness of the underlying quantities reported, remains in process.

Cause: The DHP has not developed and implemented policies and procedures to ensure that stockpile materials are appropriately and accurately captured in the financial statements. In addition, the DHP has not performed a complete assessment of operational business processes to determine the financial reporting impact and proper accounting treatment of operations.

Effect: The opening balance of the Inventory and Related Property line item is understated by the stockpile materials held by the DHP. Additionally, period expenses may be overstated by any stockpile material acquisitions that have occurred to date in FY 2019 which were not appropriately captured in recording stockpile as of September 30, 2019.

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Due to the lack of controls surrounding stockpile acquisitions and tracking, the DHP was unable to support the value of stockpile material recorded or determine the value of any misstatement.

Recommendations: Kearney recommends that the DHP:

1. Develop financial reporting policies and procedures to ensure that the DHP's operational business processes are reviewed to determine the appropriate accounting treatment, recording, and financial reporting impact.
2. Incorporate stockpile material as an assessable unit within the DHP MICP.
3. Implement policies, procedures, and controls for the end-to-end business process of stockpile materials. The policy, procedures, and controls should be developed to formally cover acquisition, receipt, issuance, transfers, inventory management, and disposal activities.
4. Establish appropriate SLAs with applicable service organizations identified within the stockpile material end-to-end lifecycle.
5. Complete ongoing efforts to verify the existence and completeness of DHP-owned stockpile material for the purpose of bringing the portfolio to record for financial reporting.
6. Complete ongoing efforts to value stockpile material in accordance with Federal accounting standards. The DHP should consider the valuation techniques within SFFAS No. 48 in establishing its opening balance of stockpile material.
7. Establish appropriate accounting policy to value new acquisitions and the consumption of existing stockpile material in accordance with SFFAS No. 3. New acquisitions should be recorded using the consumption method of accounting defined in SFFAS No. 3.

XI. Liabilities and Related Expenses (*Repeat Condition*)

Background: During the normal course of operations, Federal agencies incur certain economic events that give rise to amounts owed to external entities. These liabilities can include, among others, accounts payable (AP) for goods and services received from and progress in contract execution made by other entities excluding those services rendered by employees; Environmental and Disposal Liabilities (E&DL) for the cleanup costs associated with removing, containing, and/or disposing of hazardous waste or property that consists of hazardous; and loss contingencies for pending or threatened litigation and possible claims and assessments.

Each DHP component engages in Reimbursable Work Order – Grantor (RWO-G) transactions with its intragovernmental trading partners. In an RWO-G agreement, the DHP component grants reimbursable authority to another Federal entity that performs the work stipulated in the agreement and bills the DHP component in order to replenish the funding that it expended on the component's behalf.

Purchase cards are Government-issued credit cards that can be used for authorized Government purchases only. The purchase cardholder must reconcile component system transactions to a monthly bank credit card statement for review and approval. DHP components are responsible for developing procedures to ensure that purchase card obligations and payments are

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appropriately and accurately recorded for financial reporting purposes. In December 2018, one SMA component changed its purchase card vendor in alignment with its Military Department. The change in vendor impacted purchase card operations as a result of a non-working interface between the purchase card vendor and the SMA component GL system.

The Federal Employees Compensation Act (FECA) actuarial liability includes the expected liability for death, disability, medical, and other approved costs. The Department of Labor (DOL) administers FECA and sends Federal agencies the actuarial liability estimates for future workers' compensation benefits. In addition, DOL makes actual payments for workers' compensation benefits and then sends annual bills to the employing agencies in the chargeback process.

Condition: The DHP does not sufficiently account for its liabilities and related expenses. Specifically, the DHP and its components have not completely recorded estimated AP and expenses for goods and services received but not yet billed in accordance with SFFAS No. 5.

The DHP components do not have a process for validating receipt and acceptance of goods and services received from its intragovernmental trading partners prior to payment or a process to validate intragovernmental payment activity when receipt and acceptance cannot be performed prior to payment.

One SMA component was unable to record FY 2019 obligations, expenses, or AP transactions within its GL for any purchase card transactions from December 2018 to June 5, 2019 due to interface issues experienced during the transition to a new purchase card vendor. During December 2018 through the end of May 2019, this component's monthly bank statement reconciliation key control was not operating effectively, and no mitigating internal control was implemented to properly account for the purchase card activity.

The DHP has not sufficiently recorded other classes of liabilities and lacks internal control activities to help ensure the proper accounting of liabilities. The following transaction classes were either not completely considered by the DHP components or were not consistently recorded across components:

- Contingent or actual liabilities and related expenses
- E&DL and the related expense
- FECA liabilities, both actuarial and actual
- Prospective payments received in advance of care provided.

Cause: DHP components have not designed and implemented an effective internal control within respective procurement processes to ensure goods and services received but not yet paid for are appropriately accrued. Additionally, DHP components do not have a process in place to validate post-payment activity when receipt and acceptance cannot be performed.

For unrecorded purchase card transactions, the new purchase card vendor for the applicable Military Department did not implement the necessary system changes requested to allow the

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component GL and bank to interface properly. The interface issues were resolved as of June 6, 2019; however, the DHP component did not provide additional supporting documentation to demonstrate that purchase card activity from December 2018 through the end of May 2019 was appropriately recorded. The DHP component did not design and implement compensating internal control activities to properly reconcile purchase card activity with the bank and properly record the corresponding transactions for financial reporting.

For E&DL, settlements and judgments, and FECA, DHP components lacked policies and procedures to gather appropriate information to determine whether liabilities exist which should be reported or an appropriate assessment had not been performed to determine the reporting responsibility between DHP components and each respective Military Department.

Effect: The lack of Enterprise-wide policies and guidance has resulted in inconsistent accounting treatment across the SMAs, as well as noncompliance with Federal accounting standards and, accordingly, the FFMIA. The DHP is unable to determine whether its liabilities, net costs, and changes in net position were complete and fairly stated in accordance with GAAP.

Specific to purchase card activity, understatements may exist within the DHP financial statements pertaining to obligations within the SBR, expenses on the Statement of Net Cost, and AP on the balance sheet. The DHP did not provide documentation to determine the extent of any possible misstatement.

In situations where Military Departments pay for amounts on behalf of respective SMAs, there is risk of a potential augmentation of the DHP appropriation and violation of the Antideficiency Act.

Recommendations: Kearney recommends that the DHP:

1. Conduct a comprehensive analysis of business processes that give rise to liabilities, including unrecorded AP at the end of an accounting period, to determine whether there are unrecorded liabilities and expenses.
2. Analyze, evaluate, document, and update, as appropriate, policies and procedures to require the execution of internal control activities for the complete and accurate recording of liabilities, including AP and any estimates needed for goods and services received but not recorded.
3. Document estimate methodology for any liability estimates developed by the DHP and its components. The DHP should also implement internal control activities for estimate development and monitoring of the accuracy of the estimate.
4. Coordinate with trading partners to ensure Support Agreements (SA), Inter-Agency Agreements (IAA), MOUs, or equivalent include language requiring cooperation of the trading partner to provide any required documentation necessary for DHP components to validate the accuracy of the amounts they have been billed.
5. Retroactively complete all monthly purchase card reconciliation controls not performed while the interface issue was ongoing to ensure that purchase card activity is properly reviewed and approved.

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6. Prepare a correcting entry JV package summarizing the total dollar amount of purchase card-related accounting entry omissions and ensure that relevant personnel review and approve this correcting JV package for completeness and accuracy.
7. Collaborate with the Office of General Counsel (OGC); determine and document the legislative basis by which the Military Departments pay for E&DL, settlements and judgments, and FECA on behalf of SMA components, as applicable; and evaluate whether amounts are being charged to the correct appropriation. If any amounts are being charged to an incorrect appropriation, the DHP should evaluate the purpose statute and related concepts regarding augmentation of an appropriation and report any Antideficiency Act violations in accordance with applicable reporting requirements.

XII. Monitoring and Reporting of Obligations (*New Condition*)

Background: As part of the financial reporting process, entities perform financial analysis, reconciliations, and other internal control procedures to evaluate the validity and accuracy of financial information. DHP components review and evaluate the status and accuracy of recorded commitments, unliquidated obligations (ULO), AP, unfilled customer orders (UFCO), and AR on a triannual basis as part of the Tri-Annual Review (TAR) process (referred to as Dormant Account Review Quarterly [DARQ] beginning in FY 2020). The TAR process is required by the DoD FMR, in part, to increase each DoD component's ability to use available appropriations before they expire and to ensure remaining open obligations are liquidated before canceling.

Through the TAR process, balances are reviewed to determine if dormant balances exist and remain valid. Financial reporting personnel perform analyses over obligation activity and, if amounts are determined as stale, follow-up actions are taken with contract close-out personnel/reimbursable agreement trading partners to achieve necessary de-obligations.

Condition: The DHP's TAR process is not operating effectively to review, assess, and close stale obligations on a timely basis or has not been fully implemented across all components.

For one DHP component, a validation of the completeness and accuracy of open balances utilized in the TAR process was not performed to ensure all appropriate balances were subject to review.

The DHP responses from one component did not provide sufficient evidence to demonstrate the validity and accuracy of obligation and recovery transaction activity. Requests for documentation supporting selected open obligation and recovery transactions for testwork were either incomplete, untimely, or not clearly associated with the transaction amounts or pertinent data elements.

Cause: The DHP's TAR process has not been effectively designed or implemented across all components. DHP components have not all designed a sufficient reporting capability for ULOs or status of funds review, which has inhibited a complete and fully implemented TAR process, as required by the DoD FMR. In addition, the TAR process has not been designed to fully capture

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the DHP's open obligation activity, as certain obligation classes have not been incorporated in the process.

DHP components have not all implemented effective monitoring procedures as part of the respective internal control programs to assess the operational effectiveness of controls in place to monitor obligation activity. The DHP has not sufficiently enforced the de-obligation actions which must coincide with the detection of stale obligations. While stale obligations are being detected by the current program (i.e., marked for adjustment), the resulting de-obligation actions are not being performed timely. Certain open obligation activity requires correspondence with external parties to resolve the contracts identified as cancelled, expired, and dormant. Nonresponsive vendors and/or trading partners may add significant delays to the close-out process. Additionally, contracts under audit by outside entities contribute to delays in closing contracts, as the contracts must remain open until the external audit is completed.

Appropriate levels of information and communication in the control environment is not sufficient to be able to establish effective and timely monitoring and examination activities. The audit response function for one DHP component is not effective to timely and efficiently respond to information and documentation requests. Process owners sometimes do not respond to audit liaison personnel, respond untimely, or do not provide sufficient information.

Effect: The DHP is unable to ensure that its obligation activity is valid and accurately reported in the GL systems for all DHP components. The lack of timely action to de-obligate funds results in stale obligations remaining on the DHP's financial statements, which increases the risk of overstatement of obligated balances as presented within the SMA-Navy's SBR. As a result, the DHP's financial statements may be misstated due to dormant balances that have not been subject to review and removal. Furthermore, this prevents the DHP from utilizing available appropriations before they expire, validating ULOs prior to the cancellation of the appropriation, and returning funds to the Treasury timely.

Recommendations: Kearney recommends that the DHP:

1. Establish formalized policy and procedures for the TAR process as prescribed by OUSD(C). The formal policy should prescribe timeframes for de-obligation actions after identification and how to handle contracts prolonged in the contract close-out process.
2. Provide appropriate notification and training based on updated policy and/or revisions to the TAR process. The DHP should disseminate the new requirements to appropriate personnel across the components.
3. Establish standard queries in applicable GL systems to be able to produce financial reports which can be used as part of the TAR process. The financial report developed should reconcile to the trial balance produced from each respective GL system as a starting point to the review.
4. Perform a full-scope analysis of open obligations which are dormant and require de-obligation. The analysis can be performed in phases (e.g., greater than three years dormant, two years dormant, one year dormant); inform commands of the de-

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obligation initiative and establish cut-off dates for mandatory de-obligation; and process the de-obligation actions to remove the stale obligations.

5. Expand the MICP, as appropriate, at the component level to include testing to determine whether the TAR has been performed effectively, including tracing supporting documentation to the GL and verifying that sufficient analysis has been performed to substantiate applicable certifications.

XIII. Information Systems (*Repeat Condition*)

Background: The DHP operates a complex information system environment to execute its mission and record transactions timely and accurately using several accounting systems and a mixture of health information technology (IT) and non-medical systems. This includes third-party systems owned and operated by organizations outside of the DHP that affect the Enterprise's business processes and financial statements.

Because of the sensitive nature of the DHP's information system environment, Kearney does not present specific details related to the systems, conditions, or criteria discussed within this material weakness. We provided those details separately to DHP management and relevant stakeholders through Notices of Findings and Recommendations (NFR).

Condition: The DHP has control deficiencies in the design, implementation, and operating effectiveness of internal controls related to financially significant systems which could have a material effect on the financial statements. Internal control deficiencies exist in 26 financially significant systems, including five GL and financial reporting systems, four health IT systems, and other key feeder systems and environments. The following is a summary of critical deficiencies:

- Access Controls
  - Incomplete, inconsistent, or not fully implemented policies and procedures for managing and monitoring access to key financial management applications and third-party systems of privileged and non-privileged users
  - Incomplete and/or inconsistent implementation of user account recertifications to verify the continued propriety of access of privileged and non-privileged users
  - Incomplete or not fully implemented policies and procedures for the proper segregation of duties within applications, databases, and operating systems
- System and Services Acquisition
  - Incomplete, inconsistent, or not fully implemented policies and procedures for monitoring service organizations and implementing CUECs
- Audit and Accountability
  - Incomplete, inconsistent, or not fully implemented logging and monitoring of activity for key financial management systems.

Cause: While the DHP made progress in addressing some items noted in the prior year, the remediation efforts are ongoing and evolving as the DHA organization structure changes. The deficiencies noted above result from a multitude of causal factors, with the most pervasive ones

being the lack of complete and consistent IT policies and procedures; inconsistent or inadequate control design, implementation, and/or performance; and system limitations that prevent or hinder the implementation of effective controls. Specifically, the conditions noted above occurred primarily due to a combination of the following reasons:

- Policies and Procedures
  - Policies and procedures relevant to the control area were not developed
  - Policies and procedures were developed but were incomplete in one or more area
- Control Design and Implementation
  - Controls were not implemented during FY 2019
  - Controls were implemented but were not suitably designed to achieve the relevant control objective
  - Controls were implemented but not operating effectively during FY 2019
- System Limitation
  - The legacy system was not designed with controls in mind and cannot produce complete, detailed user listings and audit logs.

Effect: Without complete policies and procedures, and consistent implementation, IT control weaknesses may exist and be overlooked. Without sufficient controls throughout the information system environment, users may possess or retain unauthorized access to systems, as well as intentionally or unintentionally abuse computer resources, process unauthorized program changes or transactions, or perform other actions that jeopardize the confidentiality, integrity, or availability of systems and data.

Recommendations: Kearney recommends that the DHP:

1. Strengthen overall IT governance by providing guidance and oversight to the DHP components, MTFs, and service organizations on the assignment of responsibilities for the consistent implementation of internal controls.
2. Communicate IT policies and procedures to the DHP components, MTFs, and service organizations.
3. Provide training to users and privileged users regarding the consistent implementation of new IT security policy, procedures, and practices for DHP systems.
4. Monitor implementation of entity-level IT policy, procedures, and practices throughout the organization, as well as adjust training and communication where needed.
5. Ensure future system acquisitions and development:
   a. Reinforce DoD requirements that new IT systems include required IT security and privacy controls.
   b. Include requirements for financial auditability and accountability that include basic IT controls, such as audit logs, monitoring, and reporting.

* * * * *

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APPENDIX A: STATUS OF PRIOR-YEAR FINDINGS

In the *Independent Auditor's Report on Internal Control over Financial Reporting* included with the audit report on the Defense Health Program's (DHP) fiscal year (FY) 2018 financial statements, we noted several issues that were related to internal control over financial reporting. The status of the FY 2018 internal control findings is summarized in ***Exhibit 1***.

Exhibit 1: Status of Prior-Year Findings

Control Deficiency	FY 2018 Status	FY 2019 Status
Governance Structure and Entity-Level Controls	Material Weakness	Material Weakness
Financial Reporting – Compilation	Material Weakness	Resolved
Financial Reporting – Universe of Transaction Reconciliations	Material Weakness	Material Weakness
Financial Reporting – Defense Departmental Reporting System Adjustments	Material Weakness	Material Weakness
Fund Balance with Treasury	Material Weakness	Material Weakness
Medical Revenue and Associated Receivables	Material Weakness	Material Weakness
General Equipment Existence and Completeness	Material Weakness	Material Weakness
Valuation of Property, Plant and Equipment	Material Weakness	Material Weakness
Real Property	Material Weakness	Material Weakness
Internal Use Software and Internal Use Software In-Development	Material Weakness	Material Weakness
Operating Material and Supplies and Stockpile Material	Material Weakness	Material Weakness
Liabilities	Material Weakness	Material Weakness
Information Systems	Material Weakness	Material Weakness

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH LAWS, REGULATIONS, CONTRACTS, AND GRANT AGREEMENTS

To the Assistant Secretary of Defense for Health Affairs and Inspector General of the Department of Defense

We were engaged to audit, in accordance with the auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and Office of Management and Budget (OMB) Bulletin No. 19-03, *Audit Requirements for Federal Financial Statements*, the financial statements of the Defense Health Program (DHP) as of and for the year ended September 30, 2019, and the related notes to the financial statements, which collectively comprise the DHP's financial statements, and we have issued our report thereon dated November 8, 2019. Our report disclaims an opinion on such financial statements because we were unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. The DHP also asserted to departures from generally accepted accounting principles.

Compliance and Other Matters

In connection with our engagement to audit the financial statements of the DHP, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and provisions referred to in Section 803(a) of the Federal Financial Management Improvement Act of 1996 (FFMIA). We limited our tests of compliance to these provisions and did not test compliance with all laws, regulations, contracts, and grant agreements applicable to the DHP. However, providing an opinion on compliance with those provisions was not an objective of our engagement; accordingly, we do not express such an opinion. The results of our tests, exclusive of those referred to in the FFMIA, disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and OMB Bulletin No. 19-03, which are described in the accompanying Schedule of Findings.

The results of our tests of compliance with FFMIA disclosed that the DHP's financial management systems did not comply substantially with the Federal financial management systems requirements, applicable Federal accounting standards, or application of the United States Standard General Ledger (USSGL) at the transaction level, as described in the accompanying Schedule of Findings.

Additionally, if the scope of our work had been sufficient to enable us to express opinions on the financial statements, other instances of noncompliance or other matters may have been identified and reported herein.

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The DHP's Response to Findings

The DHP's response to the findings identified in our engagement is described in a separate memorandum attached to this report in Section 2, *Financial Section*, of the Agency Financial Report. The DHP's response was not subjected to the auditing procedures applied in the engagement to audit the financial statements, and accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's compliance. This report is an integral part of an engagement to perform an audit in accordance with *Government Auditing Standards* and OMB Bulletin No. 19-03 in considering the entity's compliance. Accordingly, this communication is not suitable for any other purpose.

Alexandria, Virginia
November 8, 2019

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Schedule of Findings

Noncompliance and Other Matters

I. The Federal Managers' Financial Integrity Act of 1982 (FMFIA) (*Repeat Condition*)

Office of Management and Budget (OMB) Circular A-123, *Management's Responsibility for Enterprise Risk Management and Internal Control*, implements the requirements of the Federal Managers' Financial Integrity Act of 1982 (FMFIA). FMFIA and OMB Circular A-123 require agencies to establish a process to document, assess, and assert to the effectiveness of internal control over financial reporting.

The Defense Health Program (DHP) has not established and implemented controls in accordance with standards prescribed by the Comptroller General of the United States, as codified in the Government Accountability Office's (GAO) *Standards for Internal Control in the Federal Government* (the Green Book), as evidenced by the material weakness in the *Report on Internal Control over Financial Reporting*.

As discussed in Section I, *Accounting and Financial Reporting Governance and Entity-Level Controls*, of the *Report on Internal Control over Financial Reporting*, the audit identified the following instances of noncompliance with FMFIA and OMB Circular A-123:

- The DHP has not fully implemented processes to support the effective design and operation or evaluation of its entity-level internal controls. Due to extensive design and effectiveness failures noted, the DHP did not achieve the GAO-prescribed principles for an effective internal control system
- The DHP lacks an established organizational structure to effectively implement, direct, and oversee the assessment process across components.

II. The Federal Information Security Modernization Act of 2014 (FISMA) (*Repeat Condition*)

The Federal Information Security Modernization Act of 2014 (FISMA) requires agencies to provide information security controls commensurate with the risk and potential harm of not having those controls in place. The National Institute of Standards and Technology (NIST) publishes standards and guidelines for Federal entities to implement for non-national security systems. Deviations from NIST standards and guidelines represent departures from FISMA requirements. During our audit, we noted several deviations from NIST standards and guidelines that contributed to an overall material weakness related to information systems, as described in Section XIII, *Information Systems*, in our *Report on Internal Control over Financial Reporting*. These deviations represent the DHP's noncompliance with FISMA. By not complying with FISMA, the DHP's security controls may adversely affect the confidentiality, integrity, and availability of information and information systems.

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III. The Federal Financial Management Improvement Act of 1996 (FFMIA) (*Repeat Condition*)

The Federal Financial Management Improvement Act of 1996 (FFMIA) requires that an entity's overall financial management systems environment operate, process, and report data in a meaningful manner to support business decisions. Compliance with FFMIA is achieved through substantial compliance with the following three Section 803(a) requirements:

- Federal financial management system requirements
- Applicable Federal accounting standards
- United States Standard General Ledger (USSGL) at the transaction level.

The DHP's financial management systems do not substantially comply with the requirements within FFMIA, as asserted to by management, and as discussed below.

Federal Financial Management Systems Requirements

FFMIA requires reliable financial reporting, including the availability of timely and accurate financial information, and maintaining internal control over financial reporting and financial system security. The matters described in the Basis for Disclaimer of Opinion section in the accompanying *Independent Auditor's Report*, and the material weaknesses reported in the accompanying *Report on Internal Control over Financial Reporting*, represent noncompliance with the requirement for reliable financial reporting.

FFMIA requires financial management systems owners to implement and monitor Federal information system security controls to minimize the impact to the confidentiality, integrity, and availability of the systems and data. The primary means for Federal entities to provide these controls is the implementation and monitoring of controls defined in NIST Special Publication (SP) 800-53, *Recommended Security Controls for Federal Information Systems*. The DHP deviated from recommended controls included in NIST SP 800-53, as discussed in Section XIII, *Information Systems*, in our *Report on Internal Control over Financial Reporting*. These deviations related to security management, access controls, audit logging and monitoring, and configuration management, which represent instances of noncompliance with information security requirements.

Federal Accounting Standards

FFMIA requires that agency management systems maintain data to support reporting in accordance with Generally Accepted Accounting Principles (GAAP). As identified through our audit procedures and as noted by the DHP in Note 1, *Summary of Significant Accounting Policies*, the DHP disclosed several instances where it departed from GAAP. The DHP asserted to the following departures from GAAP:

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- Accrual accounting requirements per Statement of Federal Financial Accounting Standards (SFFAS) No. 1, *Accounting for Selected Assets and Liabilities*, and SFFAS No. 5, *Accounting for Liabilities of The Federal Government*
- Recognition and valuation requirements set forth in SFFAS No. 3, *Accounting for Inventory and Related Property*
- Liability requirements set forth in SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, and SFFAS No. 12, *Recognition of Contingent Liabilities Arising from Litigation*
- Recognition and valuation requirements set forth in SFFAS No. 6, *Accounting for Property, Plant, and Equipment*
- Revenue recognition requirements set forth in SFFAS No. 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*
- Recognition and valuation requirements set forth in SFFAS No. 10, *Accounting for Internal Use Software*
- Reporting and valuation requirements set forth in SFFAS No. 29, *Heritage Assets and Stewardship Land*
- The full cost provisions of SFFAS No. 4, *Managerial Cost Accounting Standards and Concepts*, as amended by SFFAS No. 55, *Amending Inter-Entity Cost Provisions*
- Accounting and reporting requirements associated with deposit fund activity per SFFAS No. 31, *Accounting for Fiduciary Activities*
- Reporting requirements set forth in SFFAS No. 42, *Deferred Maintenance and Repairs: Amending Statements of Federal Financial Accounting Standards 6, 14, 29, and 32.*

USSGL at the Transaction Level

FFMIA requires that agency management systems record financial events by applying the USSGL guidance in the Treasury Financial Manual (TFM) at the transaction level. The DHP's financial management systems do not always record financial events in accordance with the requirements of USSGL at the transaction level. The DHP has not complied with USSGL requirements in the following instances:

- The DHP uses core accounting systems, which, for certain components, are not fully compliant with USSGL. Specifically, such accounting systems do not:
  - Accumulate or transmit complete and accurate attribute data to support financial reporting requirements
  - Possess General Ledger Account Codes (GLAC) which match standard USSGL accounts correctly in all instances and require a crosswalk for reporting
- The DHP's financial statements contain material unsupported adjustments processed and recorded during financial statement compilation procedures. The unsupported adjustments do not contain sufficient supporting documentation and/or underlying source data for recording financial events in accordance with USSGL requirements at the transaction level
- The DHP did not accumulate expenses for stockpile material in accordance with USSGL requirements. The DHP recorded stockpile material as operating expenses within the

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core accounting system. For additional details, see Section X, *Operating Materials and Supplies (OM&S) and Stockpile Material*, in our *Report on Internal Control over Financial Reporting*

- Property, Plant, and Equipment (PP&E) capital expenditures were recorded as operating expenses within the core accounting system. The DHP was unable to separately identify capitalized expenses from non-capital expenses to appropriately record internal use software (IUS) expenditures in accordance with USSGL requirements. For additional details, see Section IX, *IUS and IUS In-Development*, in our *Report on Internal Control over Financial Reporting*
- The DHP did not consistently track and accumulate revenue and accounts receivable data to post general ledger (GL) transactions consistent with USSGL requirements. The DHP had revenue and accounts receivable transactions recorded in subsidiary systems which were not recorded in the GL. For additional details, see Section V, *Medical Revenue and Associated Receivables*, in our *Report on Internal Control over Financial Reporting*
- The DHP's financial statements included summarized amounts for revenue associated with patient care provided for which no underlying transactional activity is maintained.

IV. The Debt Collection Improvement Act of 1996 (DCIA) (*Repeat Condition*)

The Debt Collection Improvement Act of 1996 (DCIA), as amended by the Digital Accountability and Transparency Act of 2014 (DATA Act), requires that any non-tax debt or claim owed to the U.S. Government that is over 120 days delinquent, is required to be reported to the Department of the Treasury (Treasury) for purposes of administrative offset. The DHP did not transfer all outstanding eligible debt in accordance with DCIA requirements. The DHP had debts that were not referred to Treasury despite exceeding the delinquency threshold of 120 days.

As discussed in Section V, *Medical Revenue and Associated Receivables*, of the *Report on Internal Control over Financial Reporting*, not all DHP components are able to support the validity of debt balances associated with medical services provided, which are recorded in the DHP's subsidiary billing and collection system. The internal control weaknesses described demonstrate an increased risk for the DHP to be fully compliant with the requirements of the DCIA. The DHP's inability to sufficiently support the validity of recorded debts limited the extent of audit procedures which could be performed over DCIA requirements.

V. The Antideficiency Act (ADA) (*New Condition*)

The Antideficiency Act (ADA) prohibits Federal agencies from: 1) making or authorizing an expenditure from, or creating or authorizing an obligation under, any appropriation or fund in excess of the amount available in the appropriation or fund unless authorized by law; 2) involving the Government in any obligation to pay money before funds have been appropriated for that purpose, unless otherwise allowed by law; or 3) making obligations or expenditures in excess of an apportionment or reapportionment or in excess of the amount permitted by agency regulations. Per 31 United States Code (U.S.C.) §1351, management is required to immediately report violations to the President and Congress, including all relevant facts and a statement of

actions taken, as well as transmit a copy of each report to the Comptroller General on the same date.

DHP management has identified one potential violation of the ADA, which is in a preliminary review/formal investigation state. This potential violation consists of purpose violations as described above; however, the reporting deadline of the internal preliminary review/formal investigation was not complete as of the date of this report.

* * * * *

Response to Independent Auditor's Report

OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE

1200 DEFENSE PENTAGON
WASHINGTON, DC 20301-1200

HEALTH AFFAIRS

NOV 0 8 2019

To: Engagement Partner, Kearney and Company, P.C.
From: Defense Health Program

Subject: Management's Response to the Independent Auditor's Report of the Defense Health Program Financial Statement Audit for Fiscal Year 2019

Thank you for the Independent Auditor's Report on the Defense Health Program (DHP)'s Consolidated Financial Statement for FY 2019 and FY 2018 and the Reports on Internal Control and Compliance with Laws and Regulations. DHP has reviewed the Auditor's Report prepared by Kearney and Company, P.C. and concurs with the Disclaimer of Opinion audit result. In its second full scope audit, DHP continued identifying areas of opportunity for improvement throughout the organization.

DHP acknowledges the material weaknesses as identified in the Report on Internal Controls over Financial Reporting and findings identified in the Compliance with Laws, Regulations, Contracts, and Grant Agreements. Despite the complexities of disparate financial systems and associated processes, management will continue working with our stakeholders to correct, improve and sustain progress of our components' financial reporting. DHP will also continue its efforts to review operational data, internal controls, and system controls necessary to ensure accuracy of the financial statements and support a strong internal control environment. As evidence of our efforts and successes in this area, we note the Defense Health Agency-Contract Resource Management (DHA-CRM), DHP's largest budgetary component, has received an unmodified (clean) audit opinion for ten consecutive years.

In FY 2019 DHP successfully remediated 15 Notifications of Findings and Recommendations (NFRs) – 12% of the total NFRs from the FY 2018 audit and a scope limitation around the definition of DHP as a Reporting Entity. Going forward, DHP is confident that with persistent commitment and investment in its financial management community, it will be well positioned to achieve continued improvements in FY 2020 and beyond based upon the valuable information we received through the FY 2019 and FY 2018 audits.

DHP heavily values its obligation to the American taxpayer to be good stewards of the resources entrusted to us to support the health of our armed forces and their families. DHP will continue to implement corrective actions to improve financial processes, systems, internal controls, and accountability of equipment as it works toward a clean audit opinion for the remaining DHP components.

DHP looks forward to working collaboratively with the Office of Inspector General and the Independent Public Accountant in the years ahead to further strengthen DHP's financial management and internal control environments.

Signed

Darrell W. Landreaux, SES
Deputy Assistant Secretary of Defense
Health Resource Management & Policy
(HRM&P)

Principal Financial Statements and Notes

These financial statements have been prepared to report the financial position, results of operations, net position, and budgetary resources of DHP, as required by the Chief Financial Officers Act of 1990, expanded by the Government Management Reform Act (GMRA) of 1994, other appropriate legislation, and in accordance with the form and content provided by OMB Circular A-136, *Financial Reporting Requirements*.

The responsibility for the integrity of the financial information contained within these statements rests with DHP management. Kearney & Company, P.C. (Kearney) was the independent public accountant engaged to audit these financial statements. The Independent Auditor's Report accompanies the principal financial statements and notes.

A brief description of the nature of each required financial statement and the related notes are listed below.

Consolidated Balance Sheets

The Balance Sheets present amounts of current and future economic benefits owned or managed by DHP (assets), amounts owed by DHP (liabilities), and residual amounts which constitute the difference (net position).

Consolidated Statements of Net Cost

The Statements of Net Cost presents the net costs of operations for the four program areas established in the DHP's strategic plan. It also presents reimbursable costs related to services provided to other federal agencies and incurred costs that are not part of DHP's core mission.

Consolidated Statements of Changes in Net Position

The Statements of Changes in Net Position reports the changes in net position during the period. Net position is affected by changes to its two components, unexpended appropriations and cumulative results of operations.

Combined Statements of Budgetary Resources

The Statements of Budgetary Resources provides information about DHP's budgetary resources, status of budgetary resources, and net outlays. The DHP's budgetary resources consist of appropriations and spending authority from offsetting collections. Budgetary resources provide DHP its authority to incur financial obligations that will ultimately result in outlays.

Notes to Financial Statements

Notes to the financial statements communicate information essential for fair presentation of the financial statements that is not displayed on the face of the financial statement.

Balance Sheets

Department of Defense

Defense Health Program

Consolidated Balance Sheets as of September 30, 2019 and 2018

(dollars in thousands)

	Unaudited	
	FY 2019	FY 2018
ASSETS (Note 2)		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	$ 19,580,243	$ 20,533,206
Accounts Receivable (Note 5)	205,699	463,605
Total Intragovernmental Assets	$ 19,785,942	$ 20,996,811
Cash and Other Monetary Assets (Note 4)	144	2,236
Accounts Receivable, Net (Note 5)	737,754	701,933
Inventory and Related Property, Net (Note 6)	52,070	32,461
General, Property, Plant, and Equipment, Net (Note 7)	3,224,053	3,725,741
Other Assets (Note 8)	33,171	29,306
TOTAL ASSETS	**$ 23,833,134**	**$ 25,488,488**
STEWARDSHIP PROPERTY, PLANT, AND EQUIPMENT (Note 1)		
LIABILITIES (Note 9)		
Intragovernmental:		
Accounts Payable	$ 183,689	$ 324,986
Other Liabilities (Notes 10, 11, and 12)	98,834	98,933
Total Intragovernmental Liabilities	$ 282,523	$ 423,919
Accounts Payable	932,604	676,201
Military Retirement and Other Federal Employment Benefits (Note 10)	256,703,184	251,338,190
Accrued Unfunded Annual Leave (Note 9)	321,277	335,237
Accrued Funded Payroll and Benefits (Note 9)	226,146	215,602
Environmental and Disposal Liabilities (Note 11)	18,098	15,566
Other Liabilities (Notes 10, 11, 12, and 13)	86,121	34,118
TOTAL LIABILITIES	**$ 258,569,953**	**$ 253,038,833**
Commitments and Contingencies (Note 14)		
NET POSITION		
Unexpended Appropriations	$ 18,603,336	$ 19,243,749
Cumulative Results of Operations	(253,340,155)	(246,794,094)
TOTAL NET POSITION	**$ (234,736,819)**	**$ (227,550,345)**
TOTAL LIABILITIES AND NET POSITION	**$ 23,833,134**	**$ 25,488,488**

The accompanying notes are an integral part of the statements.

Statements of Net Cost

Department of Defense

Defense Health Program

Consolidated Statements of Net Cost for the periods ended September 30, 2019 and 2018

(dollars in thousands)

	Unaudited	
	FY 2019	***FY 2018***
PROGRAM COSTS (Note 15)		
Gross Costs	$ 41,334,493	$ 33,206,894
Operations, Readiness & Support	38,554,678	31,968,999
Procurement	584,071	463,102
Research, Development, Test & Evaluation	1,897,228	1,018,595
Family Housing & Military Construction	298,516	(243,802)
(Less: Earned Revenue)	(3,845,944)	(3,685,072)
Net Cost before Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	37,488,549	29,521,822
Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits (Note 10)	2,594,626	(279,113)
Net Program Costs Including Assumption Changes	40,083,175	29,242,709
Costs Not Assigned to Programs	-	-
(Less: Earned Revenues) Not Attributed to Programs	-	-
NET COST OF OPERATIONS	**$ 40,083,175**	**$ 29,242,709**

The accompanying notes are an integral part of the statements.

Statements of Changes in Net Position

Department of Defense

Defense Health Program

Consolidated Statements of Changes in Net Position for the periods ended September 30, 2019 and 2018

(dollars in thousands)

	Unaudited	
	FY 2019	***FY 2018***
UNEXPENDED APPROPRIATIONS		
Beginning Balance	$ 19,243,749	$ 18,951,904
Budgetary Financing Sources:		
Appropriations Received	34,500,304	35,634,199
Appropriations Transferred In/Out	(50,557)	(1,191,372)
Other Adjustments	(1,026,566)	(1,165,588)
Appropriations Used	(34,063,594)	(32,985,394)
Total Budgetary Financing Sources	(640,413)	291,845
TOTAL UNEXPENDED APPROPRIATIONS	**$ 18,603,336**	**$ 19,243,749**
CUMULATIVE RESULTS OF OPERATIONS		
Beginning Balances	$ (246,794,094)	$ (250,231,870)
Budgetary Financing Sources:		
Appropriations Used	34,063,594	32,985,394
Non-Exchange Revenue	(143)	7,771
Other Adjustments	480	(33,287)
Other Financing Sources:		
Transfers-In/Out Without Reimbursement	(743,496)	(572,060)
Imputed Financing from Costs Absorbed by Others	295,741	311,523
Other	(79,062)	(18,856)
Total Financing Sources	33,537,114	32,680,485
Net Cost of Operations	40,083,175	29,242,709
Net Change	(6,546,061)	3,437,776
TOTAL CUMULATIVE RESULTS OF OPERATIONS	**$ (253,340,155)**	**$ (246,794,094)**
TOTAL NET POSITION	**$ (234,736,819)**	**$ (227,550,345)**

The accompanying notes are an integral part of the statements.

Statements of Budgetary Resources

Department of Defense

Defense Health Program

Combined Statements of Budgetary Resources for the periods ended September 30, 2019 and 2018

(dollars in thousands)

		Unaudited		
		FY 2019		***FY 2018***
BUDGETARY RESOURCES (Note 16)				
Unobligated balance from prior year budget authority, net	$	6,087,732	$	5,752,610
Appropriations (discretionary and mandatory)		34,375,804		34,819,410
Spending Authority from offsetting collections (discretionary and mandatory)		3,895,569		3,529,955
TOTAL BUGETARY RESOURCES	**$**	**44,359,105**	**$**	**44,101,975**
STATUS OF BUDGETARY RESOURCES				
Total New obligations and upward adjustments	$	40,085,576	$	38,799,770
Unobligated balance, end of year:				
Apportioned, unexpired accounts		2,753,443		3,357,330
Exempt from apportionment, unexpired accounts		163,066		122,809
Unapportioned, unexpired accounts		-		4,799
Unexpired unobligated balance		2,916,509		3,484,938
Expired unobligated balance		1,357,020		1,817,267
Total Unobligated balance, end of year		4,273,529		5,302,205
TOTAL STATUS OF BUDGETARY RESOURCES	**$**	**44,359,105**	**$**	**44,101,975**
OUTLAYS, NET				
Total outlays, net (discretionary and mandatory)		34,376,623		32,929,101
Distributed offsetting receipts (-)		-		(7,811)
AGENCY OUTLAYS, NET (discretionary and mandatory)	**$**	**34,376,623**	**$**	**32,921,290**

The accompanying notes are an integral part of the statements.

Notes to the Financial Statements

Note 1. Summary of Significant Accounting Policies

1. A. Reporting Entity Mission and Overall Structure

In 2011, the Deputy Secretary of Defense's Task Force on Reform of the MHS led to the creation of the DHA, a CSA and a component of the DHP. In 2013, the DoD issued a directive in accordance with the Deputy Secretary of Defense memorandum formally establishing DHA as part of the DHP, which achieved full operating capability by 2015. DHP is preparing for the management and administration of MTFs, in response to the direction provided in the FY 2019 NDAA to have the administration of all MTF's transferred from the Secretaries of each military branch to the Director of the DHA, by no later than September 30, 2021. DHP will have transferred some of the MTF's to DHA control by October 1, 2019. The DHP receives its appropriation from Congress, apportioned by the OMB to the Office of the Under Secretary of Defense (Comptroller), who allots these funds to the ASD(HA). The ASD(HA) issues Funding Authorization Documents (FADs) to fund the seven financial reporting entities that exist within DHP. These seven financial reporting entities collectively support DHP's mission. With this appropriation, DHP strives to promote a medically ready force by supporting a better, stronger, and more agile MHS, providing health care support for the full range of military operations, and sustaining the health of all those entrusted to its care. The accompanying financial statements are evaluated annually to determine compliance with Statement of Federal Financial Accounting Standards (SFFAS) 47 and to ascertain whether Federal funds under the control of DHP are being appropriately consolidated into the financial statements of the enterprise, or whether identified disclosure entities or related parties are being appropriately disclosed. Any disclosure entities or related parties identified pertaining to the DHP will be discussed in Note 19, Disclosure Entities and Related Parties as they are identified. Additionally, it should be noted that military personnel from each of the military services staff the MTF's and are part of the manpower used to generate healthcare services for the DHP.

The DHP's mission is to support the delivery of integrated, affordable, and high-quality health services to its beneficiaries and to drive greater global integration.

Based on DoD Directive 5136.01, the ASD(HA) exercises authority, direction, and control over DHP and directs the use of its appropriations. For purposes of these consolidated and combined financial statements, the following seven financial reporting components comprise the DHP FSRE:

U.S. Army Medical Command (MEDCOM): MEDCOM is a major command of the U.S. Army that provides command and control of the Army's fixed-facility medical, dental, and veterinary treatment facilities, providing preventive care, medical research and development and training institutions.

Army MEDCOM is also administratively accountable for the U.S. Army Medical Research and Development Command (USAMRDC) until FY 2020. USARMDC was moved to report vertically up the chain of command of the Army Materiel Command (AMC) effective 1 OCT 2019. However, MEDCOM maintains administrative control of the entity until FY 2020. Currently the financial reporting structure is incorporated as part of the financial structure of MEDCOM. MEDCOM distributes funding to USAMRDC, and USAMRDC is currently aligned under the MEDCOM operating agency in GFEBS. USAMRDC is included as a part of the DHP Financial Statements and thus is accounted for as a consolidation entity.

The Navy Bureau of Medicine and Surgery (BUMED): Navy Medicine is a global health care network of 63,000 personnel that provide health care support to the U.S. Navy, Marine Corps, their families and veterans in high operational tempo environments, at expeditionary medical facilities, medical treatment facilities, hospitals, clinics, hospital ships and research units around the world. Navy Medicine is led by the Navy Surgeon General and its headquarters is the Navy Bureau of

Medicine and Surgery (BUMED) in Falls Church, VA. The Navy Medicine team of physicians, dentists, nurses, corpsmen, allied health providers, and support personnel also work in tandem with the Army and Air Force medical personnel and coalition forces to ensure the physical and mental wellbeing of service members and civilians. This care is provided via the Defense Health Program and coordinated by the Office of Assistant Secretary of Defense (Health Affairs) with support from the Defense Health Agency.

U.S. Air Force Medical Service (AFMS): AFMS mission is to ensure medically fit forces, provide expeditionary medics, and deliver Trusted Care to all we serve. The AFMS vision is have their supported population be the healthiest and highest performing segment of the U.S. population.

Defense Health Agency (DHA): The DHA is a joint, integrated CSA that enables MEDCOM, Navy BUMED, and the AFMS to provide a medically ready force and ready medical force to CCMDs in both peacetime and wartime. DHA leads the MHS integrated system of readiness and health to deliver the MHS Quadruple Aim: increased readiness, better health, better care, and lower cost. The DHA oversees the execution of the $34.4 billion DHP appropriation to support the delivery of integrated, affordable, and high-quality health services to the DoD's 9.5 million eligible beneficiaries. The DHA is responsible for driving greater integration of clinical and business processes across the contracted health care networks and MTFs. The DHA respects the core values its staff brings to the Agency while upholding an organizational culture that operates by six guiding principles of transparency, accountability, leading change, empowerment, nurturing, and being team oriented.

The DHA also is accountable for the National Museum of Health and Medicine (NMHM). NMHM is funded and supported by DHP Funding and the J9 DHA Research and Development Directorate and should be accounted for as a part of the DHA's Component financial statements. The DHP acknowledges the existence of the museum, however a current GAAP Departure is also acknowledged in Note 1C of the DHP AFR for the lack of Stewardship reporting of the Museum in the financial statements of DHA and DHP under Stewardship Property Reporting Requirements.

Uniformed Services University of the Health Sciences (USUHS): The mission of USUHS is to educate, train, and comprehensively prepare uniformed services health professionals, scientists, and leaders to support the Military and Public Health Systems, the national security and national defense strategies of the United States, and the readiness of our Uniformed Services.

Transitional Intermediate Management Organization (tIMO): The tIMO is a Joint Tri-Service network of healthcare facilities that provide a medically ready force and ready medical force to CCMDs in both peacetime and wartime. It supports the delivery of integrated, affordable, and high-quality health services and is responsible for driving greater integration of clinical and business processes across the NCR. This initiative is separated into two objectives: 1) Effective and efficient delivery of world-class military healthcare in the NCR; and 2) Completion of other missions as assigned to improve management, performance and efficiency of the MHS. In the 1st Quarter of 2019, NCR MD temporarily absorbed financial reporting responsibilities for six additional MTFs (Womack Army Medical Center, Keesler Medical Center, Naval Hospital Jacksonville, 628th Medical Group - Joint Base Charleston, 4th Medical Group - Seymour Johnson Clinic, 43rd Medical Squadron - Pope AF Base) as the tIMO. This organizational change was mandated by the 2019 NDAA, sections 702 and 703. The FSRE combines the funding activity of FBCH, Walter Reed National Military Medical Center (WRNMMC), the JPC, and various clinics within the Greater Washington D.C. Area, as well as the funding activities of several MTFs in the surrounding states and region.

DHA Contract Resource Management (CRM): To add value to DHA by delivering exceptional accounting, financial, and reporting services in support of the TRICARE Private Sector Healthcare and TRICARE Retail Pharmacy Refund programs.

To achieve the CRM mission, CRM enables TRICARE beneficiaries to receive healthcare services by remunerating TRICARE contractors in accordance with their contracts in a timely and accurate manner. CRM prepares an accurate accounting of the funding used to support the TRICARE Private Sector Healthcare and TRICARE Retail Pharmacy Refund programs.

1. B. Basis of Accounting and Presentation

Basis of Accounting and Presentation: The DHP's fiscal year ends September 30. These financial statements have been prepared to report the financial position, results of operations, net position, and budgetary resources of the DHP, as required by the Chief Financial Officers Act of 1990, expanded by the GMRA of 1994, and other appropriate legislation. The financial statements have been prepared from the books and records of the DHP in accordance with, and to the extent possible, U.S. GAAP promulgated by the Federal Accounting Standards Advisory Board (FASAB); OMB Circular A-136, Financial Reporting Requirements; and the DoD's *Financial Management Regulation (FMR).*

The accompanying financial statements account for all resources for which the DHP is responsible unless otherwise noted. These financial statements, where possible, reflect both accrual and budgetary accounting transactions. Under the accrual method of accounting, revenues are recognized when earned and expenses are recognized when incurred, without regard to the receipt or payment of cash. Budgetary accounting is designed to recognize the obligation of funds according to legal requirements, which in many cases is made prior to the occurrence of an accrual-based transaction. Budgetary accounting is essential for compliance with legal constraints and controls over the use of federal funds.

However, the DHP is unable to fully implement all elements of U.S. GAAP as promulgated by FASAB and the form and content requirements for federal government entities specified by OMB in Circular A-136, Financial Reporting Requirements, due to limitations of financial and nonfinancial management processes and systems of certain component entities that support the financial statements. The DHP derives reported values and information for major asset and liability categories largely from nonfinancial systems, such as logistical systems.

The DHP's components' financial management systems used by DHP are unable to meet all full accrual accounting requirements as many of their components' financial and nonfinancial feeder systems and processes were designed and implemented prior to the issuance of U.S. GAAP. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by U.S. GAAP. These systems were designed to support reporting requirements for maintaining accountability over assets, reporting the status of federal appropriations, and recording information on a budgetary basis, rather than preparing financial statements in accordance with U.S. GAAP. Although the DoD's continued effort towards full compliancy with U.S. GAAP for the accrual method of accounting is encumbered by various systems limitations and the sensitive nature of Departmental activities, the DHP continues to implement process and system improvements addressing these limitations.

The DHP financial statements and supporting trial balances are compiled from the underlying financial data and trial balances of DHP's financial statement reporting entities. The underlying data is largely derived from budgetary transactions (obligations, disbursements, and collections), from nonfinancial feeder systems, and accruals made for major items such as payroll expenses, accounts payable, and environmental liabilities.

The DHP presents *the Consolidated Balance Sheets*, *Statements of Net Costs*, and *Statement of Changes in Net Position* on a consolidated basis which is the summation of the Components less the Eliminations. *The Statement of Budgetary Resources* is presented on a combined basis which is the summation of the Components. The financial transactions are recorded on a proprietary accrual and a budgetary basis of accounting.

Elimination of Intra-Entity Transactions and Balances: Accounting standards require an entity to eliminate intra-entity activity and balances from consolidated financial statements in order to prevent overstatement for business with itself. Transactions and balances within a reporting entity (intra-entity) have been eliminated from *the Consolidated Balance Sheets, Consolidated Statements of Net Cost, and the Consolidated Statements of Changes in Net Position*. *The Combined Statements of Budgetary Resources* is presented on a combined basis; therefore, intra-entity transactions and balances have not been eliminated from these statements. Generally, seller entities within the DoD provide summary seller-side balances for revenue, accounts receivable, and unearned revenue to the buyer-side internal accounting offices. The DoD is implementing replacement systems and a standard financial information structure that will incorporate the necessary elements to enable DHP and other DoD components to correctly report, reconcile, and eliminate intragovernmental balances.

Entity and Non-Entity*:* The DHP reports both entity and non-entity assets. Entity assets are assets that the reporting entity has authority to use in its operations. Management may have authority to decide how funds are used or it may be legally obligated to use the funds a certain way. Non-entity assets are not available for use in DHP's normal operations. The DHP maintains stewardship accountability and reporting responsibilities for non-entity assets and will forward these non-entity assets to the Treasury or other federal agencies in the future. DHP records a corresponding liability for these accounts receivable, net.

Intragovernmental and Governmental Activities*:* Statement of Federal Financial Accounting Standard 1, *Accounting for Selected Assets and Liabilities*, defines Intragovernmental and Governmental assets and liabilities. Intragovernmental assets and liabilities arise from transactions among federal entities. Intragovernmental assets are claims other federal entities owe to DHP. Intragovernmental liabilities are claims DHP owes to other federal entities.

Whereas governmental assets and liabilities arise from transactions of the federal government or an entity of the federal government with public entities, sometimes referred to as nonfederal entities. The term public entities encompass domestic and foreign persons and organizations outside the U.S. Government. Governmental assets are claims of DHP against public entities. Governmental liabilities are amounts that DHP owes to public entities.

The DHP's proportionate share of public debt and related expenses of the Federal Government is not included. The Federal Government does not apportion debt and its related costs to federal agencies. The DHP's financial statements do not report any public debt, interest, or source of public financing, whether from issuance of debt or tax revenues.

Generally, financing for the construction of DoD facilities is obtained through appropriations. To the extent this financing ultimately may have been obtained through the issuance of public debt, interest costs have not been capitalized since the U.S. Treasury does not allocate such costs to DoD.

Uses of Estimates: DHP's management makes assumptions and reasonable estimates in the preparation of financial statements based on current conditions which may affect the reported amounts. Actual results could differ materially from the estimated amounts.

Discretionary and Mandatory Spending: The DHP has both discretionary and mandatory spending. Discretionary spending is spending provided through an appropriations act(s). Mandatory spending is spending controlled by existing laws other than an appropriations act(s).

Classified Activities: SFFAS 56, Classified Activities, allows for certain presentations and disclosures to be modified, if needed, to prevent the disclosure of classified information. As such, information relative to classified assets, programs, and operations is excluded from the statements or otherwise aggregated and reported in such a manner that it is not discernible.

1. C. Departures from U.S. GAAP

Financial management systems and operations continue to be refined as DHP strives to record and report its financial activity in accordance with U.S. GAAP. The DHP is determining the actions required to bring its financial and nonfinancial feeder systems and processes into compliance with U.S. GAAP. One such action is the current revision of its accounting systems to record transactions based on the USSGL. The DHP has identified the following departures from U.S. GAAP, several which are pervasive problems within DoD that may not be remediated at the DHP level.

Fund Balance with Treasury (Note 1.H. and Note 3): The DHP was not able to identify its undistributed collections and disbursements or deposit funds in a timely manner because the DHP shares a Treasury Index (TI)-97 with Other Defense Organizations for Treasury reporting. In addition, the DHP was not able to record and report transactions in suspense accounts since suspense balances are not included in FBwT balances. As a result, the DHP is unable to explain discrepancies between its FBwT recorded in its general ledger accounts and the balance in the Treasury's accounts in accordance with SFFAS 1, Accounting for Selected Assets and Liabilities.

Accounts Receivable, Net and Revenue Recognition (Notes 1.E. and 1.J. and Note 5): The DHP did not have compliant processes in place to account for accounts receivable and the related revenue balances in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities*, and SFFAS 7, *Accounting for Revenue and Other Financing Sources*. The DHP recorded accounts receivable and associated revenue upon the receipt of cash, instead of when earned. Additionally, the DHP does not have an adequate process in place to accrue for pharmacy credits which it is owed but has not yet received. Finally, DHP does not have a sufficient process in place for the pre-authorization of services prior to billing, and thus receivables may not be collected in a timely manner.

The DHP did not have a formal policy and procedures in place to estimate the allowance for uncollectible accounts receivable in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities.*

Inventory and Related Property, Net (Note 1.F., 1.K., and Note 6): The DHP was not able to properly record and report inventory and other related property because its systems were not currently configured to support the management and valuation of all classes of inventory and related property in accordance with SFFAS 3*, Accounting for Inventory and Related Property.*

In addition, inventory and related property beginning balances have not been established using deemed cost as permitted by SFFAS 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials.*

General Property, Plant, and Equipment, Net (Note 1.L. and Note 7): Supportable general property, plant, and equipment, net beginning balances have not been established for facilities, equipment or internal use software using the alternative valuation methods permitted by SFFAS 50, *Establishing Opening Balances for General Property, Plant, and Equipment*.

The DHP did not have compliant processes in place to account for general property, plant, and equipment, net, at historical cost, in accordance with SFFAS 6, *Accounting for Property, Plant and Equipment* and SFFAS 10, *Accounting for Internal Use Software*.

The DHP also did not have compliant processes in place to record Construction-in-Progress (CIP) and is currently not assessing projects to determine if there are capitalizable constructions costs in accordance with SFFAS 6, *Accounting for Property, Plant and Equipment*.

The DHP has real property that meets both the reporting requirements of SFFAS 6, *Accounting for Property, Plant and Equipment* and SFFAS 50, *Establishing Opening Balances for General Property, Plant, and Equipment* and which should be included on its balance sheets, however, portions of real property are excluded due to a strategic pause implemented based on the issuance of guidance by OUSD-C that will transfer these assets to the MILDEPS that own the sites on which the real property is located.

The DHP did not have compliant processes in place to account for impairment of facilities and equipment in accordance with SFFAS 44, *Accounting for Impairment of General Property, Plant, and Equipment Remaining in Use.*

Leases (Note 1.L., Note 13): The DHP did not have compliant processes in place to account for capital and operating leases in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*, SFFAS 6, *Accounting for Property, Plant and Equipment,* and SFFAS 10, *Accounting for Internal Use Software*.

Stewardship Property, Plant, and Equipment (Note 1.N.)*:* The DHP did not have compliant processes for stewardship property, plant, and equipment which includes heritage assets to meet the disclosure requirements of SFFAS 29, *Heritage Assets and Stewardship Land.*

Accounts Payable and Expenses (Note 1.O.): The DHP did not have compliant processes in place to account for accounts payable, accruals, and the related expenses in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities,* and SFFAS 5, *Accounting for Liabilities of the Federal Government*.

Accrued Unfunded Annual Leave (Note 1.Q. and Note 9): Due to system limitations, the DHP was not able to fully recognize all its accrued leave liability in accordance with SFFAS 1, *Accounting for Selected Assets and Liabilities.*

Federal Employee's Compensation Act (FECA) Liabilities (Note 1.O. and Note 10): The DHP did not report the FECA actuarial liabilities/expenses and chargeback billings in accordance with SFFAS 5*, Accounting for Liabilities of the Federal Government*.

Environmental and Disposal Liabilities (Note 1.O. and Note 11): The DHP did not have compliant processes in place to account for cleanup cost associated with general property, plant, and equipment in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government*; SFFAS 6, *Accounting for Property, Plant and Equipment*; and Federal Financial Accounting and Auditing Technical Release 2, *Determining Probable and Reasonably Estimable for Environmental Liabilities in the Federal Government*.

While a GAAP Departure currently exists for FY 2019, once DoD Policy Memorandum (FMP #19-05) goes into effect on October 1, 2019, DHP will be compliant with GAAP beginning in FY 2020. DHP will not report in its financial statements real property that they occupy within jurisdictions of Military Department or Washington Headquarters Services (WHS). This will include all real property used and occupied by DHP. DHP may enter into Memoranda of Agreement, with the Military Department or WHS that is the installation host which transfers the right to control the use of a Military Department or WHS real property asset to DHP. The transfer of the right to control the use of the real property asset will not transfer jurisdiction and the asset will remain an asset of the Military Department or WHS acting as an installation host.

DHP is currently in the process of moving its real property and Environmental Liabilities to Military Department or WHS to align with the new policy. The DHP will continue to report any remaining Environmental Liabilities for the asset classes which remain on its books.

Commitments and Contingencies (Note 1.R. and Note 14): The DHP did not have compliant processes in place to account for contingent legal liabilities arising from pending or threatened litigation and all contracts that contained clauses, such as price escalation, awarded fee payments, and/or dispute resolution due to the limited capabilities of the automated system processes to capture potential liabilities in accordance with SFFAS 5, *Accounting for Liabilities of The Federal Government a*nd SFFAS 12, *Recognition of Contingent Liabilities Arising from Litigation: An Amendment of SFFAS 5, Accounting for Liabilities of the Federal Government.* Further, the DHP does not have compliant processes in place to report an estimate of obligations related to canceled appropriations and amounts of contractual arrangements that may require future financial obligations.

Additionally, the DHP did not have compliant processes in place to account for contingent liabilities arising from medical malpractice claims, claims brought under the Military Claims Act, and other settlements and judgments against the

components of DHP, in accordance with SFFAS 5, *as amended by SFFAS 12, Recognition of Contingent Liabilities Arising from Litigation.*

The DHP is still in the process of evaluating whether or not any treaties or other international agreements that it is party to may give rise to contingent liabilities that should be recognized or disclosed in accordance with SFFAS 5, *Accounting for Liabilities of the Federal Government.*

Consolidated Statements of Net Cost (Note 1.U. and Note 15): The DHP did not have compliant processes in place to ensure its Consolidated SNC was presented in accordance with SFFAS 4, *Managerial Cost Accounting Concepts and Standards*, and SFFAS 55, *Amending Inter-Entity Cost Provisions*.

Intra-Entity Activity: The DHP did not have compliant processes in place to account for intragovernmental transactions by customer in accordance with SFFAS 4, *Managerial Cost Accounting Concepts and Standards,* SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*, and SFFAS 55, *Amending Inter-entity Cost Provisions,* which require that an entity eliminates intra-entity activity and balances from consolidated financial statements in order to prevent overstatement for business with itself.

Fiduciary Activity: The DHP did not have a compliant process in place to identify, account for, and report DHP related deposit fund activity maintained at the DoD Agency-Wide level in its financial statements and/or disclose it in a note in accordance with SFFAS 31, *Fiduciary Activities*.

Budgetary Information: The DHP did not have compliant processes in place to account for Upward Adjustments of Prior-Year Undelivered Orders or adjust obligations for fluctuations in price in accordance with SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting*.

Deferred Maintenance and Repairs: The DHP acknowledges a departure from GAAP related to deferred maintenance and repairs. More information on this departure can be found in the related section within the Required Supplementary Information section of this document.

Non-Federal Physical Property: The DHP acknowledges a departure from GAAP related to non-federal physical property. More information on this departure can be found in the related section within the Required Supplementary Information section of this document.

1. D. Appropriations and Funds

Appropriations: The DHP receives general fund appropriations. General funds are used for financial transactions funded by congressional appropriations, including personnel, O&M, research and development, procurement, and MILCON. The DHP uses these appropriations and funds to execute its missions and subsequently report on resource usage.

Deposit Funds: The DHP maintains immaterial deposit funds. These funds are used to record amounts held temporarily until paid to the appropriate government or public entity. They are not the DHP funds and as such, are not available for the DHP operations. The DHP is acting as an agent or a custodian for funds awaiting distribution.

Parent-Child Reporting: DHP is a party to allocation transfers with other federal agencies as a transferring (parent) entity or receiving (child) entity. An allocation transfer is an entity's legal delegation of authority to obligate budget authority and outlay funds on its behalf. Generally, all financial activity related to allocation transfers (e.g. budget authority, obligations, outlays) is reported in the financial statements of the parent entity. Exceptions to this general rule apply to specific funds for which OMB has directed that all activity be reported in the financial statements of the child entity. These exceptions include U.S. Treasury-Managed Trust Funds, Executive Office of the President (EOP), and all other funds specifically designated by OMB. In addition to the specific DHP Appropriation, DHP also receives allocation transfers, as the child, and executes funds from the DoD Acquisition Workforce Development Fund (0111), the Global HIV/AIDS Initiative Fund (1030),

also known as the U.S. President's Emergency Plan for AIDS Relief (PEPFAR), and the Global Health Program (1031). The DHP also allocates funds to the DoD-VA Healthcare Sharing Incentive Fund (0165) which are funds appropriated by Congress to the Department of VA to operate DoD/VA Joint Health Care Centers.

1. E. Revenue and Other Financing Sources

Exchange and Non-exchange Revenue: The DHP classifies revenue as either exchange revenue or non-exchange revenue. Exchange revenue is derived from transactions in which the DHP provides goods and services to another party for a price; both the federal government and the other party receive value. Exchange revenue is presented on the *Consolidated Statements of Net Cost* and serves to offset the costs of goods and services. Revenue from exchange transactions is required to be recognized at the time DHP provides goods or services to the public or another government entity for a price. Non-exchange revenue is derived from the government's sovereign right to demand payment, such as specifically identifiable, legally enforceable claims. Non-exchange revenue is considered to reduce the cost of the DHP operations and is therefore reported on the *Consolidated Statements of Changes in Net Position* as a financing source. Nonexchange revenue is recognized when DHP establishes a specifically identifiable, legally enforceable claim to cash or other assets. It is recognized to the extent that the collection is probable.

Appropriations Used: Most of the DHP's operating funds are provided by congressional appropriations of budgetary authority. The DHP receives appropriations on annual, multiple fiscal year, and no-year bases. Upon expiration of an annual or multiple fiscal year appropriation, the obligated and unobligated balances retain their fiscal identity, and are maintained separately within an expired account. The unobligated balances can be used to make legitimate adjustments to prior year obligations but are otherwise not available for new obligations. Annual and multiple fiscal year appropriations are canceled at the end of the fifth fiscal year after expiration. No-year appropriations do not expire. Appropriation of budget authority is recognized as used when costs are incurred, for example, when goods and services are received, or benefits and grants are provided. When authorized by legislation, these appropriations are supplemented by revenues generated by sales of goods or services. The DHP recognizes revenue as a result of costs incurred for goods and services provided to other federal agencies and the public. In some instances, revenue is recognized when bills are issued.

Imputed Financing Sources from Cost Absorbed by Others and Imputed Cost: In certain cases, operating costs of the DHP are paid in full or in part by funds appropriated to other federal entities. The DHP includes applicable imputed costs in the *Consolidated Statements of Net Cost.* In addition, *Imputed Financing Sources* from *Cost Absorbed by Others* is recognized on the *Consolidated Statements of Changes in Net Position* as other financing source (non-exchange revenue).

The DHP has implemented SFFAS 55, *Amending Inter-Entity Cost Provisions*. SFFAS 55 permits entities to no longer recognize imputed costs and corresponding imputed financing from any non-business type activities, except for personnel benefit costs and Treasury Judgement Fund settlement costs. The DHP recognizes imputed costs only for business-type activities and other costs specifically required by OMB, including (1) employee pension, post-retirement health, and life insurance benefits; (2) post-employment benefits for terminated and inactive employees, to include unemployment and workers compensation under the Federal Employees' Compensation Act (FECA); and (3) losses in litigation proceedings.

The U.S. has cost-sharing agreements with countries having a mutual or reciprocal defense agreement, where U.S. troops are stationed, or where the U.S. Fleet is in a port (U.S. allies). However, the DHP does not report the consolidated support provided by U.S. allies for common defense and mutual security on the Consolidated Statements of Net Cost and in Note 16, Reconciliation of Net Cost of Operations to Budget.

Transfer In/(Out): Intragovernmental transfers may include budgetary resources or assets without reimbursement, are recorded at book value, and reported in the *Consolidated Statements of Changes in Net Position.*

Other Financing Sources: The DHP receives congressional appropriations as financing sources that expire annually, on a multi-year basis, or do not expire.

1. F. Recognition of Expenses

DoD policy requires that the DHP estimates expenses for major items such as payroll expenses, accounts payable, environmental liabilities, and unbilled revenue in the period in which it is incurred. Estimates are made for major items such as payroll expenses, accounts payable, environmental liabilities, and unbilled revenue. DHP acknowledges a departure from GAAP in its ability accurately estimate and accrue for accounts payable. In the case of Operating Materiel & Supplies (OM&S), operating expenses are generally recognized when OM&S items are purchased. OM&S is considered tangible personal property to be consumed in normal operations. For the DHP, OM&S encompasses pharmaceuticals, pharmaceutical medical supplies, and non-pharmaceutical medical supplies. The DoD has issued guidance under which Federal entities may expense OM&S using the purchase method of accounting rather than the consumption method. Under the consumption method, OM&S would be expensed when consumed. DHP is currently in the process of performing an assessment to determine whether it meets the criteria to expense OM&S under the purchase method as outlined in SFFAS 3, *Accounting for Inventory and Related Property*.

1. G. Transactions with Foreign Governments and International Organizations

The DHP sells services to foreign governments and international organizations under the provision of the Arms Export Control Act of 1976. Under the provisions of the Act, DoD has the authority to sell defense articles and services to foreign governments and international organizations, generally at no profit or loss to the federal government.

1. H. Fund Balance with Treasury

The U.S. Treasury Department performs cash management activities for all Federal Government agencies. The FBwT represents the DHP's right to draw funds from the Treasury for allowable expenditures. FBwT is increased by the receipt of appropriations and collections and decreased by outlays and fund transfers.

The U.S. Treasury maintains and reports fund balances at the Treasury Index appropriation level. Defense agencies, to include the DHP, are included at the Treasury Index 97 appropriation level, an aggregate level that does not provide identification of the separate defense agencies. As a result, the U.S. Treasury does not separately report on an amount for the DHP.

FBwT is classified as unobligated available, unobligated unavailable, or obligated. Unobligated funds, depending on budget authority, are generally available for new obligations in current operations. The unavailable balance represents funds that were appropriated in prior years which are unavailable to fund new and future obligations. The obligated-not-yet-disbursed balance represents amounts designated for payment of goods and services ordered but not yet received, or goods and services received but for which payments have not been made.

The DHP conducts a portion of operations overseas. Congress established a special account to handle the gains and losses from foreign currency transactions for five general fund appropriations: (1) O&M; (2) military personnel; (3) MILCON; (4) family housing O&M; and (5) family housing construction. The gains and losses are calculated as the variance between the exchange rate current at the date of payment and a budget rate established at the beginning of each fiscal year by OUSD-C. Foreign currency fluctuations related to other appropriations require adjustments to the original obligation at the time of payment. The DHP does not separately identify currency fluctuation transactions on its financial statements.

The disbursing offices of Defense Finance and Accounting Service (DFAS), the Military Departments, the U.S. Army Corps of Engineers (USACE), and the Department of State's financial service centers process the majority of the DHP's cash collections, disbursements, and adjustments worldwide. Each disbursing station prepares monthly reports to the U.S. Treasury on checks issued, electronic fund transfers, interagency transfers, and deposits.

In addition, DFAS and the USACE Finance Center submit reports to the U.S. Treasury by appropriation on interagency transfers, collections received, and disbursements issued. The U.S. Treasury records these transactions to the applicable FBwT account.

1. I. Undistributed Disbursements and Collections

Undistributed disbursements and collections represent the difference between disbursements and collections matched at the transaction level to specific obligations, payables, or receivables in the source systems and those reported by the U.S. Treasury. Supported disbursements and collections have corroborating documentation for the summary-level adjustments made to accounts payable and receivable. Unsupported disbursements and collections do not have supporting documentation for the transaction. However, both supported and unsupported adjustments may have been made to the DoD or component entity in line with DoD accounts payable and receivable trial balances prior to validating underlying transactions.

The DoD policy is to allocate supported undistributed disbursements and collections between federal and nonfederal categories based on the percentage of distributed federal and nonfederal accounts payable and accounts receivable. Supported undistributed disbursements and collections are then applied to reduce accounts payable and receivable accordingly. Unsupported undistributed disbursements are recorded as disbursements in transit and reduce nonfederal accounts payable. Unsupported undistributed collections are recorded in other liabilities due to the public.

1. J. Accounts Receivable, Net

Accounts receivable are amounts due to the DHP from other federal entities or the public. All intragovernmental amounts are considered fully collectible because claims with other federal agencies are resolved in accordance with the intragovernmental business rules; therefore, no allowance for loss provision is recognized.

The method CRM, a component of DHP, uses to calculate the percentage for bad debt allowance on the accounts receivable balances is determined by taking a 12-month average of the accounts receivable balance against the 12-month average on the write off balance per each accounts receivable category. The data from the prior 12-months is used to calculate the percentages for the allowance. Additionally, CRM has one specific account receivable category that follows a different percentage calculation rule, the "Suspended Pharmacy" category. Per a DHA PI directive that prevents CRM's Pharmacy contractor from pursuing collection action against Suspended Pharmacies while under investigation, CRM uses a 100% allowance methodology for calculating the debt against the accounts receivable balance.

The DHP is required to transfer the collection of accounts receivable at 120 days to the U.S. Treasury Department for additional collection efforts. Accounts receivable that are transferred to the U.S. Treasury Department for collection should remain on the DHP's books until the U.S. Treasury Department acknowledges that the debt is uncollectible. Once the U.S. Treasury acknowledges that the debt is uncollectible, the DHP will close out the bad debt and take it off their books.

1. K. Inventory and Related Property

The DHP inventory and related property includes stockpile materials. Stockpile materials are strategic and critical materials held due to statutory requirements or for use in national defense, conservation, or national emergencies. Stockpile materials are not held with the intent of selling in the ordinary course of business. The DHP is required to maintain various medications for the DoD in the event a medical epidemic reaches the United States. The DHP accounts for the purchase of stockpile materials using the purchase method of accounting and expenses these items upon purchase instead of when consumed.

1. L. General Property, Plant, and Equipment, Net

Per DoD Policy Memorandum (FMP #19-05), effective October 1, 2019, DHP will not report in its financial statements real property that they occupy within jurisdictions of Military Department or Washington Headquarters Services (WHS). This will include all real property used and occupied by DHP. DHP may enter into Memoranda of Agreement, with the Military Department or WHS that is the installation host which transfers the right to control the use of a Military Department or WHS real property asset to DHP. The transfer of the right to control the use of the real property asset will not transfer jurisdiction and the asset will remain an asset of the Military Department or WHS acting as an installation host.

For FY 2019, DHP is currently still in the process of moving its real property to Military Department or WHS to align with the new policy.

Capitalization Threshold: DHP's General GPP&E capitalization threshold is $250 thousand. The capitalization threshold applies to asset acquisitions and modifications/improvements placed into service after September 30, 2013. GPP&E assets acquired prior to October 1, 2013 were capitalized at prior threshold levels ($100 thousand for equipment and $20 thousand for real property) and are carried at the remaining net book value.

Depreciation Method:

Asset Classes	Depreciation/Amortization Method	Service Life
Buildings, Structures, and Facilities	S/L*	35, 40 or 45
Software	S/L	2-5 or 10
Equipment	S/L	5

**Straight line (S/L)*

Buildings, structures, and facilities: Real property in the federal government generally includes land, land improvements, buildings, facilities, and structures. The DHP does not own land or land improvements. However, for buildings, facilities, and structures, OUSD-C directed the DHP to stop reporting these types of real property assets and transfer them to the line military departments that own the installations on which they reside. DHP is in the process of transferring its remaining balances in this category.

Equipment and Software: Includes equipment, software purchased, and internal use software meeting the capitalization threshold and expected to be used in the DHP's operations. The DHP has not fully developed and executed its accounting policy and related reporting for software and internal use software.

Construction-in-Progress (CIP): DoD Policy Memorandum (FMP #19-05), effective October 1, 2019, requires that DHP components that are the funding entity for construction of an asset report CIP balances in their respective CIP accounts until the asset is placed in service. Completed CIP projects are then transferred to the respective Military Department property holder. The DHP allocates and provides oversight for all its MILCON. The USACE, and Naval Facilities and Engineering Command, and the Air Force Civil Engineering Center are the execution agents for all DHP CIP and related funds received.

Leases: The DHP has not fully developed and executed its accounting policy and related reporting requirements for its lease activity. The DHP is in the process of performing an analysis of its lease contracts, but that process has not yet been completed as of June 30, 2019.

1. M. Other Assets

Advances and Prepayments: When advances are permitted by law, legislative action, or presidential authorization, the DHP's policy is to record advances or prepayments. As such, payments made in advance of the receipt of goods and services are reported as assets on the *Consolidated Balance Sheets*. The DHP's policy is to expense and/or properly classify assets when the related goods and services are received.

1. N. Stewardship Property, Plant, and Equipment

Disclosures for stewardship property, plant, and equipment are required under SFFAS 29, *Heritage Assets and Stewardship Land*. DHP has heritage assets. Heritage assets are unique for one or more of the following reasons: (1) historical or natural significance, (2) cultural, educational, or artistic importance, or (3) significant architectural characteristics. Heritage assets are generally expected to be preserved indefinitely. The DHP operates the National Museum of Health and Medicine.

1. O. Liabilities

Liabilities represent probable and measurable amounts to be paid by the DHP because of past transactions and are recognized when incurred, regardless of whether there are budgetary resources available to pay them. However, the liquidation of these liabilities will consume budgetary resources and cannot be made until available budgetary resources have been obligated. Thus, for financial reporting purposes, the liabilities are classified as liabilities covered or not covered by budgetary resources.

Covered and Uncovered Liabilities: Liabilities incurred that are covered by available budgetary resources as of the *Consolidated Balance Sheet* date are referred to as funded liabilities. Liabilities are covered by budgetary resources if they are funded by appropriations, provided that the resources are apportioned by OMB without further action by the Congress and without a contingency having to be met first. Budgetary resources include: (1) new budget authority, (2) unobligated balances of budgetary resources at the beginning of the year or net transfers of prior-year balances during the year, (3) spending authority from offsetting collections (credited to an appropriation or fund account), and (4) recoveries of unexpired budget authority through downward adjustments of prior-year obligations.

Liabilities that are not covered by available budgetary resources as of the *Consolidated Balance Sheets* date are referred to as unfunded liabilities.

Current and Noncurrent Liabilities: The DHP segregates its other liabilities between current and noncurrent liabilities. The current liabilities represent liabilities that the DHP expects to settle within the 12 months of the Balance Sheet date. Noncurrent liabilities represent liabilities that DHP does not expect to be settled within the 12 months of the Balance Sheets date.

Accounts Payable: Accounts payable are amounts primarily owed for goods, services, or capitalized assets received, progress on contract performance by others, and other expenses due.

FECA Liabilities**:** FECA liabilities provide income and medical cost protection to covered federal civilian employees injured on the job, to employees who have incurred work-related occupational diseases, and to beneficiaries of employees whose deaths are attributable to job-related injuries or occupational diseases. The FECA program is administered by the U.S. Department of Labor (DOL), which pays valid claims against the DHP and subsequently seeks reimbursement from DHP for these paid claims. Therefore, the accrued FECA liability, included in Intragovernmental Other Liabilities, represents amounts due to DOL for claims paid on behalf of the DHP. These liabilities are not covered by budgetary resources because funding has not been made available.

In addition, the DHP recognizes an actuarial FECA liability. The actuarial FECA liability represents the liability for future workers' compensation (FWC) benefits, which includes the expected liability for death, disability, medical, and miscellaneous costs for approved cases. The liability is determined by DOL annually, as of September 30, using a method that utilizes historical benefits payment patterns related to a specific incurred period to predict the ultimate payments related to that period. Projected annual payments were discounted to present value based on OMB's interest rate assumptions, which were interpolated to reflect the average duration in years for income payments and medical payments.

To provide more specifically for the effects of inflation on the liability for FWC benefits, wage inflation factors (cost-of-living adjustment) and medical inflation factors (consumer price index – medical) are applied to the calculation of projected future benefits. The actual rates for these factors are also used to adjust the historical payments to current-year constant dollars. These liabilities are not covered by budgetary resources because funding has not been made available.

Environmental and Disposal Liabilities: The DHP has not fully developed and executed its accounting policy and related reporting for environmental and disposal liabilities. These liabilities are not covered by budgetary resources because funding has not been made available.

1. P. Military Retirement and Other Federal Employment Benefits

Military Retirement and Other Federal Employment Benefits provide income and medical benefits to covered military personnel and Federal civilian employees. These actuarial liabilities are not covered by budgetary resources because funding has not yet been made available.

The DHP implemented requirements of SFFAS 33, Pensions, *Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates*, which directs that the discount rate, underlying inflation rate, and other economic assumptions be consistent with one another. A change in the discount rate may cause other assumptions to change as well. For the September 30, 2019, financial statement valuation, the application of SFFAS 33 required DoD OACT to set the long-term inflation, the Consumer Price Index (CPI), the DHP actuarial liability is adjusted at the end of each fiscal year. The 4th Quarter, FY 2019 balance represents the September 30, 2019 amount that will be effective through 3rd quarter of FY 2020.

1. Q. Accrued Unfunded Annual Leave

Accrued leave includes salaries, wages, and other compensation earned by employees, but not disbursed as of September 30, 2019. Annually, as of September 30, the balances of accrued unfunded annual leave are adjusted to reflect current pay rates. Sick leave and other types of non-vested leave are expensed as taken. These liabilities are not covered by budgetary resources because funding has not yet been made available.

1. R. Commitments and Contingencies

A contingency is an existing condition, situation, or set of circumstances involving uncertainty as to possible gain or loss. The uncertainty will ultimately be resolved when one or more future events occur or fail to occur. SFFAS 5, *Accounting for Liabilities of the Federal Government*, as amended by SFFAS 12, *Recognition of Contingent Liabilities Arising from Litigation,* requires contingent liabilities and related expenses to be recognized when a past event has occurred, and a future outflow or other sacrifice of resources is measurable and probable. Further, SFFAS 5, as amended, requires (1) report a contingent liability on the balance sheet when an unfavorable outcome is 'probable,' and (2) disclose a contingent liability in the notes to the financial statements when an unfavorable outcome is 'reasonably possible.' No disclosure is required if the loss from a contingent liability is considered 'remote.'

A contingent legal liability arises from pending or threatened litigation, possible claims, and assessments which could result in monetary loss to an entity. The actual monetary liability in contingent legal cases can be considered case-by-case or as an aggregate of multiple cases.

The DHP's risk of loss and resultant contingent liabilities arising from pending or threatened litigation or claims and assessments are due to events such as medical malpractice, property or environmental damages, and contract disputes.

Financial statement reporting is limited to disclosure when conditions for liability recognition do not exist but there is at least a reasonable possibility of incurring a loss or additional losses. The DHP's risk of loss and resultant contingent liabilities arise from pending or threatened litigation or claims and assessments due to events such as aircraft, ship and vehicle accidents; medical malpractice; property or environmental damages; and contract disputes.

The DHP is evaluating treaties and other international agreements that may give rise to contingent liabilities and that should be recognized and disclosed in accordance with SFFAS 5 as amended by SFFAS 12.

1. S. Net Position

Net position is the residual difference between assets and liabilities and is comprised of Unexpended Appropriations and Cumulative Results of Operations.

Unexpended Appropriations: Unexpended appropriations represent the amounts of budgetary resources that are unobligated and have not been rescinded or withdrawn. Unexpended appropriations also represent amounts obligated for which legal liabilities for payments that have not been incurred.

Cumulative Results of Operations: Cumulative Results of Operations represent the net difference between expenses and losses, and financing sources (including appropriations, revenue, and gains), since inception. The cumulative results of operations also include transfers in and out of assets that were not reimbursed.

1. T. Treaties for Use of Foreign Bases

The DHP has the use of land, buildings, and other overseas facilities that are obtained through various international treaties and agreements negotiated by the Department of State. Generally, the treaty terms allow the DHP continued use of these properties until the treaties expire. The DHP purchases capital assets overseas with appropriated funds; however, the host country retains title to the land and capital improvements. In the event treaties or other agreements are terminated, use of the foreign bases is prohibited and losses are recorded for the value of any non-retrievable capital assets. The settlement due to the U.S. or host nation is negotiated and considers the value of capital investments and may be offset by the cost of the environmental cleanup.

1. U. Consolidated Statements of Net Cost

The *Consolidated Statements of Net Cost* represents the net cost of programs that are supported by appropriations or other means. The intent of the *Consolidated Statements of Net Cost* is to provide gross and net cost information related to the amount of output or outcome for a given program or organization administered by a responsible reporting entity. The DHP current processes and systems capture costs based on appropriations groups.

In FY 2019, the DoD completed implementation of SFFAS 55, *Amending Inter-entity Cost Provisions*, which rescinds SFFAS 30, *"Inter-Entity Cost Implementation: Amending SFFAS 4, Managerial Cost Accounting Standards and Concepts and Interpretation 6, Accounting for Imputed Intra-departmental Costs: An Interpretation of SFFAS 4."* The DoD is in the process of reviewing available data and developing a cost reporting methodology as required by the SFFAS 4, *Managerial Cost Accounting Concepts and Standards for the Federal Government*, as amended.

1. V. Tax Status

The DHP is not subject to federal, state, or local income taxes. Accordingly, no provision for income taxes is recorded.

1. W. Public-Private Partnerships

SFFAS 49, *Public-Private Partnerships* defines public-private partnerships as "risk-sharing arrangements or transactions with expected lives greater than five years between public and private sector entities" and is effective for FY 2019.

1. X. Significant Events

In the 1st Quarter of 2019, NCR MD temporarily absorbed financial reporting responsibilities for six additional MTFs (Womack Army Medical Center, Keesler Medical Center, Naval Hospital Jacksonville, 628th Medical Group - Joint Base Charleston, 4th Medical Group - Seymour Johnson Clinic, 43rd Medical Squadron - Pope AF Base) as the tIMO. This organizational change was mandated by the 2019 NDAA, sections 702 and 703.

Note 2. Non-Entity Assets

Non-entity assets consisted of the following as of September 30, 2019 and 2018 (*dollars in thousands)*:

	Unaudited	
	FY 2019	***FY 2018***
Intragovernmental Assets		
Accounts Receivable	$ -	$ (12)
Total Intragovernmental Assets	**$ -**	**$ (12)**
Nonfederal Assets		
Accounts Receivable	$ 1,989	$ 3,237
Total Nonfederal Assets	1,989	3,237
Total Non-Entity Assets	1,989	3,225
Total Entity Assets	23,831,145	25,485,263
Total Assets	**$ 23,833,134**	**$ 25,488,488**

Non-entity assets are not available for use in DHP's normal operations. The DHP has stewardship accountability and reporting responsibility for non-entity assets, which are included on the balance sheet.

The non-entity accounts receivable due from the public, restricted by nature, consists of refund receivables, interest receivables, penalties and fines, and the related allowance for loss on interest receivables. As receivables are collected, they are deposited to Treasury.

The DHP acknowledges various departures from U.S. GAAP as discussed in Note 1.C, *Departures from U.S. GAAP.*

Note 3. Fund Balance with Treasury

Fund balance with Treasury consisted of the following as of September 30, 2019 and 2018 (*dollars in thousands)*:

	Unaudited	
	FY 2019	*FY 2018*
Status of Fund Balance with Treasury:		
Unobligated Balance		
Available	$ 2,916,509	$ 3,480,139
Unavailable	1,357,020	1,822,066
Total Unobligated Balance	**$ 4,273,529**	**$ 5,302,205**
Obligated Balance not yet Disbursed	$ 15,868,557	$ 15,842,634
Non-Budgetary Fund Balance with Treasury		
Clearing Accounts	-	-
Deposit Funds	-	-
Non-Entity and Other	-	-
Total Status of Fund Balance with Treasury	**$ 20,142,086**	**$ 21,144,839**
Non-Fund Balance with Treasury Budgetary Accounts		
Unfilled Customer Orders Without Advance	$ (166,946)	$ (174,213)
Receivables and Other	(394,897)	(437,420)
Non-Fund Balance with Treasury Budgetary Accounts	(561,843)	(611,633)
Total Fund Balance with Treasury	**$ 19,580,243**	**$ 20,533,206**

The Treasury records cash receipts and disbursements on the DHP's behalf and are available only for the purposes for which the funds were appropriated. The DHP's fund balances with treasury consists of appropriation accounts, trust accounts, and other fund types.

The Status of FBwT reflects the budgetary resources to support FBwT and is a reconciliation between budgetary and proprietary accounts. It primarily consists of unobligated and obligated balances. The balances reflect the budgetary authority remaining for disbursement against current or future obligations.

Unobligated and obligated balances presented in this note may not equal related amounts reported on the *Combined SBR* because unobligated and obligated balances reported on the *Combined SBR* are supported by FBwT and other budgetary resources that do not affect FBwT.

Non-FBwT Budgetary Accounts reduce the Status of FBwT. This amount is comprised of unfilled customer orders without advance of $166.9 million and reimbursements and other income earned and not collected of $394.9 million.

The FBwT reported in the financial statements has been adjusted to reflect DHP's balance as reported by Treasury. The difference between FBwT in DHP's general ledgers and FBwT reflected in the Treasury accounts is attributable to transactions that have not been posted to the individual detailed accounts in DHP's general ledger as a result of timing differences or the inability to obtain valid accounting information prior to the issuance of the financial statements. When research is completed, these transactions will be recorded in the appropriate individual detailed accounts in DHP's general ledger accounts.

The DHP acknowledges departures from U.S. GAAP related to FBwT as discussed in Note 1.C, *Departures from U.S. GAAP.*

Note 4. Cash and Other Monetary Assets

Cash and other monetary assets consisted of the following as of September 30, 2019 and 2018 (*dollars in thousands)*:

	Unaudited FY 2019	FY 2018
Cash and Other Monetary Assets		
Undeposited Collections	$ 144	$ 2,236
Total Cash and Other Monetary Assets	**$ 144**	**$ 2,236**

Cash and other monetary assets reported are comprised of undeposited collections received by DHP.

Note 5. Accounts Receivable, Net

Accounts receivable, net consisted of the following as of September 30, 2019 and 2018 (*dollars in thousands*):

	Unaudited FY 2019 Gross Amount Due	Allowance For Estimated Uncollectible	Accounts Receivable, Net
Intragovernmental Receivables	$ 205,699	$ N/A	$ 205,699
Receivables due from the Public	891,718	(153,964)	737,754
Total Accounts Receivable	**$ 1,097,417**	**$ (153,964)**	**$ 943,453**

	Unaudited FY 2018 Gross Amount Due	Allowance For Estimated Uncollectible	Accounts Receivable, Net
Intragovernmental Receivables	$ 463,605	$ N/A	$ 463,605
Receivables due from the Public	844,918	(142,985)	701,933
Total Accounts Receivable	**$ 1,308,523**	**$ (142,985)**	**$ 1,165,538**

Accounts Receivable represents DHP's claim for payment from other entities. DHP only recognizes an allowance for uncollectible amounts from the public.

Intragovernmental receivables:

Represent amounts due from other federal agencies. The SMA MTFs provide medical services for TRICARE beneficiaries, including those that are dual eligible under Medicare, as well as Federal beneficiaries of the United States Coast Guard (USCG), Public Health Service (PHS), National Oceanic and Atmospheric Administration (NOAA), and Department of Veterans Affairs (VA).

Accounts receivable due from the public:

Arises from the provision of care by SMA Military Treatment Facilities (MTF)which is comprised of the following:

- Third Party Collections (TPC), relates to medical services provided to TRICARE beneficiaries with other health insurance (e.g., from their employers).
- Medical Service Accounts (MSA), Public, includes medical services provided and charged directly to eligible beneficiaries (e.g., coinsurance, copays, elective services). MSA - Public also includes emergency room visits by individuals who are not TRICARE beneficiaries or other eligible agencies.
- Medical Affirmative Claims (MAC), relates to medical services provided when another party is liable (e.g., homeowners or auto liability insurer).

Additionally, As of September 30, 2019, CRM had recorded $170.6 million related to the Standard Discount Program (SDP) and the Additional Discount Program (ADP). The SDP resulted from the implementation of the Federal Ceiling Program for the TRICARE Retail Pharmacy Refunds Program as required by the FY 2008 NDAA, Section 703. The ADP resulted from voluntary agreements between TRICARE and the pharmaceutical manufacturers providing additional discounts above the SDP.

The DHP acknowledges departures from U.S. GAAP related to accounts receivable, net as discussed in Note 1.C, *Departures from U.S. GAAP.*

Note 6. Inventory and Related Property

Inventory and related property for the period ended September 30, 2019 and 2018 (dollars in thousands):

	Unaudited	
	FY 2019	*FY 2018*
Inventory and Related Property		
Stockpile Materials, Net	$ 52,070	$ 32,461
Total Inventory and Related Property	**$ 52,070**	**$ 32,461**

Operating materials and supplies (OM&S), consist of tangible personal property to be consumed in normal operations.

Stockpile materials, consist of materials held due to statutory requirements or for use in national defense, conservation, or national emergencies.

DHP accounts for the purchase of stockpile materials using the purchase method of accounting and expenses these items upon purchase instead of when consumed. The $52.1M of stockpile recorded reflects the efforts of one DHP component which began remediation efforts to record stockpile material using the consumption method of accounting as required by SFFAS 3.

The DHP acknowledges departures from U.S. GAAP related to inventory and related property as discussed in Note 1.C, *Departures from U.S. GAAP*.

Note 7. General Property, Plant, and Equipment, Net

General property, plant, and equipment, net consisted of the following as of September 30, 2019 and 2018 (*dollars in thousands*):

	Method	Useful Life	*Unaudited FY 2019* Acquisition Value	(Accumulated Depreciation / Amortization)	Net Book Value
Major Asset Classes					
Buildings, Structures, and Facilities	S/L	35, 40 or 45	$ 5	$ -	$ 5
Software	S/L	2-5 or 10	1,225	(437)	788
General Equipment	S/L	5	1,730,441	(1,196,198)	534,243
Capital Leases (Assets)	S/L	Lease Term	2,501	(2,501)	-
Construction-in- Progress	N/A	N/A	2,689,017	-	2,689,017
Other Assets	N/A	N/A	-	-	-
Total General PP&E			**$ 4,423,189**	**$ (1,199,136)**	**$ 3,224,053**

	Method	Useful Life	*Unaudited FY 2018* Acquisition Value	(Accumulated Depreciation / Amortization)	Net Book Value
Major Asset Classes					
Buildings, Structures, and Facilities	S/L	35, 40 or 45	$ 1,556	$ -	$ 1,556
Software	S/L	2-5 or 10	393,919	(315)	393,604
General Equipment	S/L	5	1,667,477	(1,329,544)	337,933
Capital Leases (Assets)	S/L	Lease Term	-	-	-
Construction-in- Progress	N/A	N/A	2,986,507	-	2,986,507
Other Assets	N/A	N/A	19,322	(13,181)	6,141
Total General PP&E			**$ 5,068,781**	**$ (1,343,040)**	**$ 3,725,741**

Most of DHP's general property, plant, and equipment, net owned or leased by DHP is primarily used to provide high quality, cost effective health care services to active forces and other eligible beneficiaries.

Buildings, Structures, and Facilities

The DHP facilities range from sophisticated tertiary care medical centers to outpatient and dental clinics and physiological training units. Refer to 1.L. *General Property, Plant, and Equipment, Net.*

Internal Use Software

Internal Use Software identified in the schedule as "software" can be purchased from commercial vendors off-the-shelf, modified "off the shelf", internally developed, or contractor developed. Internal Use Software includes software that is used to operate programs (financial and administrative software).

MHS GENESIS is the new electronic health record system that manages military patient health information. MHS GENESIS integrates inpatient and outpatient solutions that will connect medical and dental information across the continuum of care, from point of injury to the MTF. When fully deployed, MHS GENESIS will provide a single health record for service members, veterans, and their families. The DHP acknowledges that MHS GENESIS is not presented in the balances above based on ongoing assessment of system for accounting and valuation purposes.

Equipment

Dental, surgical, radiographic, and pathologic equipment is essential to providing high quality health care services that meet accepted standards of practice. The required safety standards, related laws and regulatory requirements from credentialing and health care standard setting organizations influence and affect the requirement for, cost of, and replacement and modernization of medical equipment. The DHP also acquires and leases capital equipment for MTFs and participates in other selected health care activities such as acquiring equipment for the initial outfitting of a newly constructed, expanded, or modernized health care facility; equipment for modernization and replacement of uneconomically reparable items; equipment supporting programs such as pollution control, clinical investigation, and occupational/environmental health; and MHS information technology (IT) requirements.

Capital Leases

In providing healthcare to its patient population, the components of the Defense Health Program sometimes lease medical equipment for use within its facilities. This medical equipment consists of items such digital radiography x-ray systems and computerized axial tomography scanners.

Construction-In-Progress

The DHP often encounters the need to obtain fixed assets through the process of construction. Costs related to constructed assets of the DHP are recorded as construction-in-progress until such a time as construction is completed and the asset can either be transferred to its intended entity or place into service.

Other Disclosures

The DHP has the use of overseas facilities that are obtained through various international treaties and agreements negotiated by the Department of State. Generally, treaty terms allow DHP continued use of these properties until the treaties expire. There are no other known restrictions on general property, plant, and equipment.

Year to date depreciation and amortization expense totaled $91.1 million for the year ended, September 30, 2019.

The DHP acknowledges departures from U.S GAAP related to general property, plant, and equipment, net as discussed in Note 1.C, *Departures from U.S. GAAP.*

Note 8. Other Assets

Other assets consisted of the following as of September 30, 2019 and 2018 (*dollars in thousands)*:

	Unaudited	
	FY 2019	***FY 2018***
Non-Federal Other Assets		
Advances and Prepayments	$ 33,169	$ 29,304
Other Assets (With the Public)	2	2
Total Non-Federal Other Assets	**$ 33,171**	**$ 29,306**

Advances and Prepayments are payments made in advance for payroll and travel.

Note 9. Liabilities Not Covered by Budgetary Resources

Liabilities covered and not covered by budgetary resources consisted of the following as of September 30, 2019 and 2018 (*dollars in thousands)*:

	Unaudited	
	FY 2019	***FY 2018***
Liabilities not Covered by Budgetary Resources:		
Intragovernmental		
Other	$ 48,049	$ $47,132
Total Intragovernmental	**$ 48,049**	**$ 47,132**
Nonfederal		
Accounts Payable	$ 106,507	$ 30,895
Military Retirement and Other Federal Employment Benefits	256,703,026	251,338,190
Accrued Unfunded Annual Leave	321,278	335,237
Environmental and Disposal Liabilities	18,098	15,566
Other	46	-
Total Nonfederal	**$ 257,148,955**	**$ 251,719,888**
Total Liabilities Not Covered by Budgetary Resources	**$ 257,197,004**	**$ 251,767,020**
Total Liabilities Covered by Budgetary Resources	**$ 1,372,949**	**$ 1,271,813**
Total Liabilities	**$ 258,569,953**	**$ 253,038,833**

Liabilities not covered by budgetary resources are liabilities not currently funded by existing budgetary authority as of the balance sheet date. Budgetary authority to satisfy these liabilities is expected to be provided in a future Defense Appropriations Act.

Intragovernmental Liabilities – Other

These consists primarily of unfunded liabilities for Federal Employees' Compensation Act, Judgement Fund and unemployment compensation.

Non-Federal Liabilities – Accounts Payable

Primarily represents liabilities in canceled appropriations, which if paid, will be disbursed using current year funds.

Non-Federal Liabilities – Military Retirement and Other Federal Employment Benefits

These consists of various employee actuarial liabilities not due and payable during the current fiscal year. Refer to Note 10, Military Retirement and Other Federal Employment Benefits, for additional details and disclosures.

Non-Federal Liabilities – Environmental and Disposal Liabilities

Represents DHP's liability for existing and estimates related to future events for environmental and clean-up and disposal. Refer to Note 11, Environmental and Disposal Liabilities, for additional details and disclosures.

Accrued Unfunded Annual Leave

Represents the DHP's estimated liability at the end of the current period for earned but unpaid and unfunded annual leave.

Nonfederal – Other

Represents various contingent liability amounts booked by AFMS.

The DHP acknowledges departures from U.S. GAAP related to various liabilities as discussed in Note 1.C, *Departures from U.S. GAAP*.

Note 10. Military Retirement and Other Federal Employment Benefits

Military retirement and other federal employment benefits consisted of the following as of September 30, 2019 and 2018 (*dollars in thousands)*:

	Unaudited	
	FY 2019	***FY 2018***
	Unfunded Liabilities	
Pension and Health Benefits		
Military Pre Medicare-Eligible Retiree Health Benefits	$ 254,832,838	$ 249,693,998
Total Pension and Health Benefits	**$ 254,832,838**	**$ 249,693,998**
Other Benefits		
FECA	$ 196,464	$ 213,964
Other	1,673,882	1,430,228
Total Other Benefits	**$ 1,870,346**	**$ 1,644,192**
Total Military Retirement and Other Federal Employment Benefits	**$ 256,703,184**	**$ 251,338,190**

The Actuarial Liability consists of the following as of September 30, 2019 and 2018 (dollars in thousands):

	Unaudited	
	FY 2019	***FY 2018***
	Military Pre Medicare-Eligible Retiree Health Benefits	
Beginning Actuarial Liability	$ 249,693,998	$ 252,512,861
Expenses		
Normal Cost	10,357,828	10,135,672
Interest Cost	9,166,847	9,772,839
Plan Amendments	-	(2,678,284)
Actuarial Experience Gains	(6,049,443)	(8,729,912)
Other Factors	-	(1)
Total Expenses before Gains from Actuarial Assumptions Changes	**$ 13,475,232**	**$ 8,500,314**
Actuarial Assumption Changes		
Changes in Trend Assumptions	(232,024)	(3,804,999)
Changes in Assumptions Other than Trend	2,826,650	3,525,886
Total (gains) from Actuarial Assumption Changes	**$ 2,594,626**	**$ (279,113)**
Total Expenses	**$ 16,069,858**	**$ 8,221,201**
Less: Benefit Outlays	10,931,018	11,040,064
Total Changes in Actuarial Liability	**$ 5,138,840**	**$ (2,818,863)**
Ending Actuarial Liability	**$ 254,832,838**	**$ 249,693,998**

Military Retirement and Other Federal Employment Benefits provide income and medical benefits to covered military personnel and Federal civilian employees. These actuarial liabilities are not covered by budgetary resources because funding has not yet been made available. The DoD OACT calculates this actuarial liability at the end of each fiscal year using the current active and retired population plus assumptions about future demographic and economic conditions.

The schedules above reflect two distinct types of liabilities related to Military Retirement and Other Federal Employment Benefits. The line entitled “Military Pre Medicare-Eligible Retiree Health Benefits” represents the actuarial (or accrued) liability for future health care benefits provided to non-Medicare-eligible retired beneficiaries that are not yet incurred. The line entitled “Other” includes two reserves, a small retiree life insurance reserve ($225 thousand in FY 2019) for a closed group of USUHS retirees and the IBNR, which is an estimate of benefits already incurred but not yet reported to DoD for all DHP beneficiaries (excluding those from the retiree population who are Medicare-eligible).

The DHP implemented requirements of SFFAS 33, Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions and Selecting Discount Rates and Valuation Dates, which directs that the discount rate, underlying inflation rate, and other economic assumptions be consistent with one another. A change in the discount rate may cause other assumptions to change as well. For the September 30, 2019, financial statement valuation, the application of SFFAS 33 required DoD OACT to set the long-term inflation, the CPI to be consistent with the underlying Treasury spot rates used in the valuation. The DHP actuarial liability is adjusted at the end of each fiscal year. The 4th Quarter, FY 2019 balance represents the September 30, 2019 amount that will be effective through 3rd quarter of FY 2020.

Actuarial Cost Method: As prescribed by SFFAS 5, the valuation of the Military Retirement Health Benefits is performed using the Aggregate Entry Age Normal (AEAN) cost method. AEAN is a method whereby projected retiree medical plan costs are spread over the projected service of a new entrant cohort.

Assumptions*:* For the FY 2019 financial-statement valuation, the long-term assumptions include a 3.5% discount rate and medical trend rates that were developed using a 1.8% inflation assumption. Note that the term 'discount rate' refers to the interest rate used to discount cash flows. The terms 'interest rate' and 'discount rate' are often used interchangeably in this context.

For the FY 2018 financial-statement valuation, the long-term assumptions included a 3.6% discount rate and medical trend rates that were developed using a 1.5% inflation assumption.

The change in the long-term assumptions is due to the application of SFFAS 33. This applicable financial statement standard is discussed further below. Other assumptions used to calculate the actuarial liabilities, such as mortality and retirement rates, were based on a blend of actual experience and future expectations. Because of reporting deadlines and as permitted by SFFAS 33, the current year actuarial liability is rolled forward from the prior year valuation results using accepted actuarial methods. This roll-forward process is applied annually. In calculating the FY 2019 "rolled-forward" actuarial liability, the following assumptions were used:

Discount Rate	**3.5%**	
Inflation	**1.8%**	
Medical Trend (Non-Medicare)	**FY 2018 – FY 2019**	**Ultimate Rate FY 2043**
Direct Care Inpatient	4.00%	4.05%
Direct Care Outpatient	5.50%	4.05%
Direct Care Prescription Drugs	6.00%	4.05%
Purchased Care Inpatient	2.50%	4.05%
Purchased Care Outpatient	3.25%	4.05%
Purchased Care Prescription Drugs	5.69%	4.05%
Purchased Care USFHP	3.97%	4.05%

After a 25 year select period, an ultimate trend rate is assumed for all future projection years.

The DHP's actuarial liability increased $5.1 billion (2.1%). This resulted from the net effect of: an increase of $ 8.6 billion due to expected increases (interest cost plus normal cost less benefit outlays), an increase of $2.6 billion due to changes in key assumptions; no plan changes; and a decrease of $6.0 billion due to actual experience being different from what was assumed (demographic and claims data).

DoD complies with SFFAS 33. The standard requires the separate presentation of gains and losses from changes in long-term assumptions used to estimate liabilities associated with pensions, other retirement and other postemployment benefits. SFFAS 33 also provides a standard for selecting the discount rate and valuation date used in estimating these

liabilities. SFFAS 33, as published on October 14, 2008, by the FASAB requires the use of a yield curve based on marketable U.S. Treasury Securities to determine the discount rates used to calculate actuarial liabilities for federal financial statements. Historical experience is the basis for expectations about future trends in marketable Treasury securities.

The statement is effective for periods beginning after September 30, 2009 and applies to information provided in general purpose federal financial statements. It does not affect statutory or other special-purpose reports, such as Pension or Other Retirement Benefit reports. SFFAS 33 requires a minimum of five periodic rates for the yield curve input and consistency in the number of historical rates used from period to period. It permits the use of a single average discount rate if the resulting present value is not materially different from what would be obtained using the yield curve.

For the September 30, 2019 financial-statement valuation, DoD OACT determined a single equivalent discount rate of 3.5% by using a 10-year average of quarterly zero-coupon Treasury spot rates. These spot rates are based on the U.S. Department of the Treasury – Office of Economic Policy's 10-year Average Yield Curve for Treasury Nominal Coupon Issues (TNC yield curve), which represents average rates from April 1, 2009 through March 31, 2019.

The DHP acknowledges departures from U.S. GAAP related to FECA liabilities as discussed in Note 1.C, *Departures from U.S. GAAP.*

Note 11. Environmental and Disposal Liabilities

Environmental and Disposal Liabilities consisted of the following as of September 30, 2019 and 2018 (*dollars in thousands)*:

	Unaudited	
	FY 2019	***FY 2018***
Environmental Liabilities—Nonfederal		
Nuclear Powered Military Equipment / Spent Nuclear Fuel	$ 16,854	$ 15,497
Other Accrued Environmental Liabilities - Non-BRAC	1,244	69
Total Environmental Liabilities	**$ 18,098**	**$ 15,566**

Applicable laws and regulations for cleanup requirements:

(a) Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA)
(b) Superfund Amendments and Reauthorization Act (SARA)
(c) Clean Water Act
(d) Safe Drinking Water Act
(e) Clean Air Act
(f) Resource Conversation and Recovery Act (RCRA)
(g) Toxic Substances Control Act (TSCA)
(h) Medical Waste Tracking Act
(i) Atomic Energy Act
(j) Nuclear Waste Policy Act
(k) Low Level Radioactive Waste Policy Amendments Act

The DHP is required to clean up contamination from past waste disposal practices, leaks, spills, and other activity resulting in public health or environmental risk. The DHP accomplishes this effort in coordination with regulatory agencies and, if applicable, other responsible parties and current property owners. The DHP is also required to recognize closure and post-closure costs for its general property, plant, and equipment, and environmental corrective action costs for current operations. Each of DHP's major reporting entities is responsible for tracking and reporting all required environmental information related to environmental restoration costs, other accrued environmental costs, disposal costs of weapon systems, and environmental costs related to BRAC actions.

The DHP follows the CERCLA, Superfund Amendments and Reauthorization Act of 1986 (SARA, Public Law 99-499), Resource Conservation and Recovery Act (RCRA, Public Law 94-580) or other applicable federal or state laws to clean up contamination. The CERCLA and RCRA require DHP to clean up contamination in coordination with regulatory agencies, current owners of property damaged by DHP and third parties with partial responsibility for environmental restoration. Failure to comply with agreements and legal mandates puts DHP at risk of incurring fines and penalties.

The Nuclear Waste Policy Act of 1982 (Public Law 97-425) requires owners and generators of high-level nuclear waste and spent nuclear fuel to pay their share of the cost of the program. The Low-Level Radioactive Waste Policy Amendments Act of 1985 (Public Law 99-240) provides for the safe and efficient management of low-level radioactive waste.

For DHP the types of environmental liabilities and disposal liabilities are identified as nuclear or non-nuclear. Nuclear liabilities arise from a research reactor and irradiators. Non-nuclear liability arises from medical and chemical cleanup.

The DHP is not aware of any pending changes but the liability can change in the future due to changes in laws and regulations, changes in agreements with regulatory agencies, and advances in technology.

Accounting estimates for environmental liabilities use reasonable judgments and assumptions based on available information. Actual results may materially vary if agreements with regulatory agencies require remediation to a different degree than anticipated when calculating the estimates. Liabilities can be further affected if investigation of the environmental sites reveals contamination levels differing from estimate parameters. The DHP tangible property, plant, and equipment contains nonfriable asbestos. At this time, the DHP is unable to reasonably estimate the clean-up costs related to removal and some environmental liabilities.

The DHP acknowledges departures from U.S GAAP related to environmental and disposal liabilities as discussed in Note 1.C, *Departures from U.S. GAAP*.

Note 12. Other Liabilities

Other liabilities consisted of the following as of September 30, 2019 and 2018 (*dollars in thousands*):

	Unaudited FY 2019 Current Liability	Noncurrent Liability	Total
Other Liabilities			
Intragovernmental			
Advances from Others	$ 15,803	$ -	$ 15,803
FECA Reimbursements due to DOL	20,979	25,684	46,663
Employer Contribution and Payroll Taxes Payable	32,994	-	32,994
Other Liabilities	3,374	-	3,374
Total Intragovernmental Other Liabilities	**$ 73,150**	**$ 25,684**	**$ 98,834**
Due to the Public			
Advances from Others	$ 54,394	$ 2,591	$ 56,985
Employer Contribution and Payroll Taxes Payable	22,009	-	22,009
Other Liabilities	7,080	47	7,127
Total Due to the Public Other Liabilities	**$ 83,483**	**$ 2,638**	**$ 86,121**
Total Other Liabilities	**$ 156,633**	**$ 28,322**	**$ 184,955**

	Unaudited FY 2018 Current Liability	Noncurrent Liability	Total
Other Liabilities			
Intragovernmental			
Advances from Others	$ 13,967	$ -	$ 13,967
FECA Reimbursements due to DOL	19,761	26,250	46,011
Employer Contribution and Payroll Taxes Payable	34,345	-	34,345
Other Liabilities	4,514	96	4,610
Total Intragovernmental Other Liabilities	**$ 72,587**	**$ 26,346**	**$ 98,933**
Due to the Public			
Advances from Others	$ 3,663	$ 3,434	$ 7,097
Employer Contribution and Payroll Taxes Payable	20,274	-	20,274
Other Liabilities	6,745	2	6,747
Total Due to the Public Other Liabilities	**$ 30,682**	**$ 3,436**	**$ 34,118**
Total Other Liabilities	**$ 103,269**	**$ 29,782**	**$ 133,051**

Advances from Others

The balance represents liabilities for collections received to cover future expenses or acquisition of assets.

Federal Employee's Compensation Act (FECA) Reimbursement to the DOL

The balance represents liabilities due under the Federal Employee Compensation Act. The liability includes amounts for unbilled incurred and estimated accruals. Refer to Note 10, Military Retirement and Other Federal Employment Benefits, for the estimated FECA actuarial liability.

The DHP acknowledges departures from U.S. GAAP related to FECA reimbursements as discussed in Note 1.C, *Departures from U.S. GAAP*.

Custodial Liabilities

This balance represents liabilities for collections reported as non-exchange revenues where DHP is acting on behalf of another Federal entity.

Employer Contributions and Payroll Taxes Payable

This balance represents the employer portion of payroll taxes and benefit contributions for health benefits, retirement, life insurance and voluntary separation incentive payments.

Intragovernmental Other Liabilities

This balance primarily consists of unemployment compensation liabilities.

Accrued Funded Payroll and Benefits

This includes accrued funded payroll of $226.1M and unfunded annual leave liability of $321.3M that fluctuates quarter to quarter based on use of annual leave by civilian personnel and is what primarily makes up the balance of the other liabilities line of this note.

Environmental Liability

This is a part of the Non-Environmental Disposal liability related to the final disposition of equipment, munitions, and other national defense weapon systems that are considered non-nuclear. Disposal measurements involve the use of cost estimates that consider the anticipated level of effort required to dispose of the item.

Note 13. Leases

Leases consisted of the following as of September 30, 2019 and 2018 respectively (dollars in thousands):

ENTITY AS LESSEE-Capital Leases	*Unaudited* FY 2019	FY 2018
Land and Buildings	$ 2,501	$ -
Machinery and Equipment	-	-
Other	-	-
Accumulated Amortization	(2,501)	-
Total Assets Under Capital Leases	**$ -**	**$ -**

Future payments due under operating leases consisted of the following as of September 30, 2019 (dollars in thousands):

ENTITY AS LESSEE-Operating Leases	*Unaudited* Asset Category Buildings and Equipment		
Future Payments Due For Non-Cancellable Operating Leases			
Fiscal Year	**Federal Future Leases Payments**	**Non-Federal Future Leases Payments**	**Total Future Leases Payments**
2020	$ -	$ 6,956	$ 6,956
2021	-	23,440	23,440
2022	-	24,453	24,453
2023	-	24,934	24,934
2024	-	25,815	25,815
After 5 Years	-	26,727	26,727
Total Future Lease Payments	**$ -**	**$ 132,325**	**$ 132,325**

The DHP acknowledges departures from U.S. GAAP related to leases as discussed in Note 1.C., Departures from U.S. GAAP.

Note 14. Commitments and Contingencies

DHP is a party to various administrative proceedings and legal actions related to healthcare claims payments, accidents, environmental damage, equal opportunity matters and contractual bid protests which may ultimately result in settlements or decisions adverse to the federal government. These proceedings and actions arise in the normal course of operations and their ultimate disposition is unknown.

Amounts disclosed for litigation claims and assessments are fully supportable and agree with DHP's legal representation letters and management summary schedule.

DHP will disclose an estimate of obligations related to cancelled appropriations for which the DHP has a contractual commitment for payment and amounts for contractual arrangements which may require future financial obligations, when there are any.

DHP will disclose amounts for potential future obligations such as contractual arrangements for fixed price contracts with escalation, price redetermination, or incentive clauses; contracts authorizing variations in quantities; and contracts where allowable interest may become payable based on contractor claims under the "Disputes" clause contained in contracts, when there are any. Amounts disclosed will represent future potential liabilities and will not include amounts already recognized as contingent liabilities. Consideration will be given in disclosing the difference between the maximum or ceiling amounts and those amounts recognized when it is reasonably possible the maximum amount may be paid.

Additionally, DHP is advised that there are situations where counsel was not able to express an opinion concerning the likely outcome of a case. As such, the DHP did not make an estimate of any probable or reasonably possible loss contingencies through its respective legal counsel.

Furthermore, medical malpractice claims and settlements arising from the activities of the Navy BUMED, AFMS, and MEDCOM are paid either by funds appropriated directly to the military service lines and/or the Department of Treasury's Judgement Fund.

The DHP cannot estimate the amount of undelivered orders for open contracts citing cancelled appropriations.

DHP acknowledges departures from U.S GAAP related to the commitment and contingencies as discussed in Note 1.C, Departures from U.S. GAAP.

Note 15. Disclosures Related to the Statements of Net Cost

Department of Defense

Defense Health Program

Consolidated Statement of Net Cost for the year ended September 30, 2019 and 2018

(dollars in thousands)

	Unaudited	
	FY 2019	*FY 2018*
Program Costs		
Operations, Readiness and Support		
Gross Costs	$ 38,554,678	$ 31,968,999
Less: Earned Revenue	(3,803,713)	(3,635,239)
Net Program Cost	$ 34,750,965	$ 28,333,760
Procurement		
Gross Cost	$ 584,071	$ 463,102
Less: Earned Revenue	(16,335)	(6,494)
Net Program Cost	$ 567,736	$ 456,608
Research, Development, Test and Evaluation		
Gross Cost	$ 1,897,228	$ 1,018,595
Less: Earned Revenue	(25,895)	(43,339)
Net Program Cost	$ 1,871,333	$ 975,256
Family Housing and Military Construction		
Gross Cost	$ 298,516	$ (243,802)
Less: Earned Revenue	-	-
Net Program Cost	$ 298,516	$ (243,802)
Total Gross Costs	**$ 41,334,493**	**$ 33,206,894**
Less: Total Earned Revenue	(3,845,944)	(3,685,072)
Net Program Costs	$ 37,488,549	$ 29,521,822
Gain on pension, ORB, or OPED Assumption Changes (Note 10)	2,594,626	(279,113)
NET COST OF OPERATIONS	**$ 40,083,175**	**$ 29,242,709**

The DoD's current processes and systems capture costs based on appropriations groups as presented in the schedule above. The lower level costs for major programs are not presented as required by the Government Performance and Results Act. The DoD is in the process of reviewing available data and developing a cost reporting methodology as required by the SFFAS 4, Managerial Cost Accounting Concepts and Standards for the Federal Government, as amended by SFFAS 55, Amending Inter-Entity Cost Provisions.

Effective FY 2018, DHP elected early implementation of SFFAS 55 which rescinds SFFAS 30, Inter-Entity Cost Implementation: Amending SFFAS 4, Managerial Cost Accounting Standards and Concepts and Interpretation 6, Accounting for Imputed Intra-Departmental Costs: An Interpretation of SFFAS 4.

DHP accounting systems generally do not capture information relative to heritage assets separately and distinctly from normal operations.

DHP's Military Retirement and post-employment costs are reported in accordance with SFFAS 33, Pensions, Other Retirement Benefits, and Other Postemployment Benefits: Reporting the Gains and Losses from Changes in Assumptions

and Selecting Discount Rates and Valuation Dates. The standard requires the separate presentation of gains and losses from changes in long-term assumptions used to estimate liabilities associated with pensions, other retirement and other postemployment benefits on the SNC.

DHP acknowledges departures from U.S GAAP related to managerial cost accounting as discussed in Note 1.C, Departures from U.S. GAAP.

Inter-Entity Costs

DHP has instances where goods and services are received from other federal entities at no cost or at a cost less than the full cost to the providing federal entity. Consistent with SFFAS 55, DHP recognizes imputed costs only for business-type activities and other costs specifically required by OMB, including (1) employee pension, post-retirement health, and life insurance benefits; (2) post-employment benefits for terminated and inactive employees, to include unemployment and workers compensation under the Federal Employees' Compensation Act (FECA); and (3) losses in litigation proceedings.

Goods and services are received from other federal entities at no cost or at a cost less than the full cost to the providing federal entity. Consistent with accounting standards, certain costs of the providing entity that are not fully reimbursed by DHP are recognized as imputed costs in the SNC and are offset by imputed revenue in the SCNP. Such imputed costs and revenues relate to business-type activities, employee benefits, and claims to be settled by the Treasury Judgment Fund.

However, unreimbursed costs of goods and services other than those identified above are not included in our financial statements.

Note 16. Disclosures Related to the Combined Statement of Budgetary Resources

Disclosures related to the *SBR* consisted of the following for the periods ended September 30, 2019 and 2018:

Undelivered Orders at End of the Period

Undelivered orders (UDOs) consist of goods and services obligated that have been ordered but not received. Unpaid UDOs represent obligations for goods and services that have not been received or paid. Whereas, paid UDOs represent obligations for goods and services that have been paid for in advance of receipt. The budgetary resources obligated for UDOs for the quarter ended, September 30, 2019, consisted of (*dollars in thousands*):

	Unaudited	
	FY 2019	***FY 2018***
Undelivered Orders		
Intragovernmental		
Undelivered orders – unpaid	$ 2,621,985	$ 4,815,357
Total Intragovernmental Undelivered Orders	**$ 2,621,985**	**$ 4,815,357**
With the Public		
Undelivered orders – unpaid	$ 11,944,600	$ 9,776,635
Undelivered orders – paid	33,169	29,304
Total Undelivered Orders with the Public	**$ 11,977,769**	**$ 9,805,939**
Total Undelivered Orders	**$ 14,599,754**	**$ 14,621,296**

Legal Arrangements Affecting the Use of Unobligated Balances

Information about legal limitations and restrictions affecting the use of the unobligated balance of budget authority is specifically stated by program and fiscal year in the applicable appropriation language or in the alternative provisions section at the end of the appropriations act.

The use of unobligated balances is restricted based on annual legislation requirements and other enabling authorities. Funds are appropriated on an annual, multi-year, no-year, and subsequent year basis. Appropriated funds shall expire on the last day of availability and are no longer available for new obligations. Unobligated balances in unexpired fund symbols are available in the next fiscal year for new obligations unless some restrictions had been placed on those funds by law. Amounts in expired fund symbols are unavailable for new obligations, but may be used to adjust previously established obligations.

Explanation of Differences between the *Consolidated Statement of Budgetary Resources* and the Budget of the U.S. Government

The reconciliation between the Combined SBR and the Budget of the U.S. Government (Budget) is presented below. The U.S. Government Budget amounts used in the reconciliation below represents the FY 2018 balances. The U.S. Government Budget amounts for FY 2019 will be available in early February 2020 at OMB website http://www.whitehouse.gov/omb/budget) and will be available in early February 2020.

Budget of the U.S. Government (dollars in millions)

Unaudited FY 2018	Budgetary Resources	Obligations Incurred	Distributed Offsetting Receipts	Net Outlays, Net
Combined Statement of Budgetary Resources	$ 44,102	$ 38,799	$ (8)	$ 32,929
Shared Appropriations with Others included in the SBR but excluded from DHP direct appropriations presented in the President's Budget	(1,552)	-	-	-
Unobligated Balance Brought Forward from prior year included in the SBR but not included in the President's Budget	(2,362)	-	-	-
Other	(5)	(1,478)	4	(632)
Budget of the U.S. Government	**$ 40,183**	**$ 37,321**	**$ (4)**	**$ 32,297**

Explanation of Differences between the *Consolidated Statement of Changes in Net Position* and the *Combined Statement of Budgetary Resources*

The 'Appropriations' line on the Combined SBR does not agree with the 'Appropriations received' line on the Consolidated SCNP due to: 1) differences between proprietary and budgetary accounting concepts and reporting requirements; and 2) presentation of the Consolidated SCNP on a consolidated basis versus presentation of Combined SBR on a combined basis.

Note 17. Reconciliation of Net Cost to Net Outlays

Effective for FY 2019, the FASAB issued SFFAS 53, Budget and Accrual Reconciliation, which requires a reconciliation of net outlays on a budgetary basis to its net cost of operations (reported on an accrual basis) during the reporting period. The Budget and Accrual Reconciliation replaces the Statement of Financing (SOF) note disclosure. OMB Circular No. A-136, Financial Reporting Requirements indicates that comparative presentation for the prior year is not required in the initial year of implementation. The analysis only displays information for the reporting period for the Year Ended September 30, 2019.

Budgetary and financial accounting information differ. Budgetary accounting is used for planning and control purposes and relates to both the receipt and use of cash, as well as reporting the federal deficit. Financial accounting is intended to provide a picture of the government's financial operations and financial position, so it presents information on an accrual basis. The accrual basis includes information about costs arising from the consumption of assets and the incurrence of liabilities. The reconciliation of net outlays, presented on a budgetary basis, and the net cost, presented on an accrual basis, provides an explanation of the relationship between budgetary and financial accounting information. The reconciliation serves not only to identify costs paid for in the past and those that will be paid in the future, but also to assure integrity between budgetary and financial accounting. The analysis below illustrates this reconciliation by listing the key differences between net cost and net outlays.

The Reconciliation of Net Cost to Net Outlays below explains how budgetary resources outlaid during the period relate to the net cost of operations for DHP.

Budget and Accrual Reconciliation as of September 30, 2019 (*dollars in thousands*):

	Unaudited FY 2019		
	Intragovernmental	With the Public	Total
Net Operating Cost	$ **1,137,227**	$ **38,945,948**	$ **40,083,175**
Components of Net Cost That are not Part of Net Outlays			
Property, Plant, and equipment depreciation	$ -	$ (91,085)	$ (91,085)
Property, plant, and equipment disposal and revaluation	-	(621)	(621)
Other	-	(572,433)	(572,433)
Increase/(Decrease) in Assets:			
Accounts Receivable	$ (257,890)	$ 35,820	$ (222,070)
Other Assets	-	1,774	1,774
Increase/(Decrease) in Liabilities			
Accounts Payable	$ (31,183)	$ (62,368)	$ (93,551)
Salaries and Benefits	1,508	(12,438)	(10,930)
Environmental and Disposal Liabilities	-	(2,532)	(2,532)
Other Liabilities (Unfunded leave, Unfunded FECA, Actuarial FECA)	320	(5,424,728)	(5,424,408)
Other Financing Sources			
Federal Employee retirement benefit costs paid by OPM and imputed to the agency	(295,741)	-	(295,741)
Transfers Out/(In) Without Reimbursement	743,496	-	743,496
Total Components of Net Costs that Are Not Part of Net Outlays	**$ 160,510**	**$ (6,128,611)**	**$ (5,968,101)**
Components of Net Outlays That are not Part of Net Costs			
Acquisition of Capital Assets	$ -	$ 282,436	$ 282,436
Other	-	(143)	(143)
Total Components of Net Outlays That are not Part of Net Costs	**$ -**	**$ 282,293**	**$ 282,293**
Net Outlays	**$ 1,297,737**	**$ 33,099,630**	**$ 34,397,367**
Outlays, Net, From Statements of Budgetary Resources			**34,376,623**
Reconciling Difference			**$ (20,744)**

Net Cost of Operations: is derived from the SNC.

Components of net cost that are not part of net outlays: are most commonly (a) the result of allocating assets to expenses over more than one reporting period (e.g., depreciation) and the write-down of assets (due to revaluations), (b) the temporary timing differences between outlays/receipts and the operating expense/revenue during the period, and (c) costs financed by other entities (imputed inter-entity costs).

Components of net outlays that are not part of net cost: are primarily amounts provided in the current reporting period that fund costs incurred in prior years and amounts incurred for goods or services that have been capitalized on the balance sheet (e.g., plant, property and equipment acquisition and inventory acquisition).

Due to DHP's financial system limitations, budgetary resources obligated during the period could not be reconciled to DHP Net Cost of Operations. The difference is a previously identified deficiency.

Other financing sources: include a limited number of special transactions that are used to account for non-operating revenues/receipts and expenditures/disbursements.

Other temporary timing differences: reflect special adjustments (e.g., prior period adjustments due to correction of errors).

Net Outlays: is the summation of Net Cost of Operations, Components of net cost that are not part of net outlays, Components of net outlays that are not part of net cost and other temporary timing differences and equals the SBR net outlays amount.

Reconciling Difference: represents the difference between the amount of net outlays as calculated by the Budget and Accrual Reconciliation presented above and Line 4210 of DHP's Statement of Budgetary Resources. Currently, DHP is unable to determine the exact cause of the reconciling difference but has been able to determine that it is related to future account mapping adjustments that will need to be made in its financial systems to accommodate differences in accounting by specific components of the DHP.

Note 18. Public-Private Partnerships

In FY 2019 DHP performed an assessment and did not identify public-private partnerships that meet the requirement of SFFAS 49.

Note 19. Disclosure Entities and Related Parties

DHP has implemented SFFAS 47, Reporting Entity. This standard defines the Federal Reporting Entity as inclusive of the consolidation entity, disclosure entities, and related parties. DHP consolidation entity includes accounts administratively assigned by the OMB to the DHP in the Budget of the U.S. Government. DHP consolidation entity did not change as a result of SFFAS 47 implementation. Consolidation accounts reported in FY 2018 are consistent with accounts reported within DHP financial statements for FY 2019. DHP also has disclosure entities which are similar to consolidation entities, however they have a greater degree of autonomy with the Federal Government than a consolidation entity.

DHP has identified one related party, Henry M. Jackson Foundation for the Advancement of Military Medicine (HJF).

HJF is an independent, incorporated, 501(c)3 non-profit corporation that was established by Congress in 1983. The purpose of the Foundation is to carry out medical research and education projects under cooperative arrangements with the USUHS, to serve as a focus for the interchange between military and civilian medical personnel, and to encourage the participation of the medical, dental, nursing, veterinary, and other biomedical sciences in the work of the Foundation for the mutual benefit of military and civilian medicine. The President of the USUHS serves as an ex-officio member of the HJF's Council of Directors and holds the ability to influence the financial and operational policy decisions of the HJF.

DHP also participates in a cooperative agreement with HJF related to the collection of royalty revenues which opens the DHP to the potential for gain or risk of loss due to the fact that under this agreement royalty revenues due to the USUHS, may be held and collected by HJF in endowment funds. This exposes USUHS, a component of the DHP, to the potential risk of misuse or improper accounting treatment of these funds while in the possession of HJF.

DHP also identified eight disclosure activities:

DoD Acquisition Workforce Development Fund, Transfer Account

The DAWDF was established under 10 USC 1075. The law requires that not more than 30 days after the end of the first quarter of each fiscal year, the head of each military department and Defense Agency shall remit to the Secretary of Defense, from amounts available to such military department or Defense Agency, as the case may be, for contract services for O&M, an amount equal to the applicable percentage for such fiscal year. The applicable percentage for a fiscal year is the percentage that results in the credit to the Fund of $500,000,000 in such fiscal year. This amount may be adjusted by the Secretary of Defense (SECDEF). DHP transfers money to this fund as mandated by federal law but has no other control. The purpose of the DAWDF is to ensure the DoD acquisition workforce (AWF) has the capacity, in both personnel and skills, needed to (1) properly perform its mission; (2) provide appropriate oversight of contractor performance; and (3) ensure

that the Department receives the best value for the expenditure of public resources. Given that the components of the DHP make use of DoD acquisition personnel, their transfer of funds in support of this program provides them with these same potential benefits as well.

DoD-VA Health Care Sharing Incentive Fund (JIF), Transfer Account

Public law requires a $15M transfer of DHP funds annually under Section 8111 of Title 38 of the US Code and Section 721 of Public Law 107-314 (NDAA for FY 2003). This fund is managed and reported by the Department of VA and DHP has no control outside of the annual fund transfer required by law. The money in this fund provides seed money and incentives for innovative DoD/VA joint sharing initiatives to recapture purchased care, improve quality and drive cost savings at facilities, regional and national levels. The DHP is allowed to partake in these initiatives and as such is afforded the potential to obtain these same benefits. The DHP transferred $15 million in funding to this program during FY 2019.

Global Health Programs, State

The DoD's global health engagement efforts are part of a whole-of-government approach, conducted in close coordination with other U.S. Government agencies, including the Department of State, Department of Health and Human Services, Department of Agriculture, and the United States Agency for International Development (USAID). DHP transfers money to contribute to this effort on an annual basis but has no other elements of control.

Global HIV/ADIS Initiative, Transfer Account

The DoD HIV/AIDS Prevention Program (DHAPP), based at the Naval Health Research Center (NHRC) in San Diego, California, is the DoD Executive Agent for the technical assistance, management, and administrative support of the global HIV/AIDS prevention, care, and treatment for foreign militaries. DHAPP administers funding, directly conducts training, and provides technical assistance for focus countries and other bilateral countries, and has staff actively serving on most of the Technical Working Groups and Core Teams through the Office of the U.S. Global AIDS Coordinator. DHAPP oversees the contributions to PEPFAR of a variety of DoD organizations, which fall under the various regional military commands, as well as specialized DoD institutions whose primary mission falls within the continental United States.

Defensive Institute for Medical Operations

The Defense Institute for Medical Operations (DIMO) is a dual-service agency comprised of Air Force and Navy personnel committed to providing world class, globally-focused, healthcare education and training to partners around the world. DIMO utilizes subject matter experts (SMEs) throughout the DoD to develop curriculum and teach courses around the world. Upon review of the DIMO fact sheet available on the entity website, it was noted that this program was realigned under the AFMS from the DSCA in 2010. Upon discussion with DIMO personnel, they stated that DIMO receives an immaterial amount of DHP funding ($302K) transferred to them using the 2X fund code to support two GS Personnel at DIMO warranting disclosure within the DHP financial statements.

Fisher House Foundation

The Fisher House Foundation is an independent not for profit organization which occasionally receives a small amount of money from DHA issued grants in order to construct new houses for families on the sites of MTFs and VA medical centers.

James Lovell Federal Health Center

This health care facility located in North Chicago, Illinois is a joint venture between Navy BUMED and the VA established by Section 1704 of Public Law 111-84 (NDAA for FY 2010). DHP transfers money to this fund based on public law but the facility itself is independently managed by a joint DoD/VA management board of directors as directed by law. DHP has no administrative control. In FY 2019, DHP transferred $113.0 million to the joint DoD-VA Demonstration Fund in support of the operations of this healthcare facility.

Medicare-Eligible Retiree Health Care Fund

A portion of receipts from the MERCHF accrual fund are transferred into the DHP O&M account annually as outlined in the DHP budget justification. The fund is managed and appropriated independently of the DHP.

Note 20. Insurance Programs

Insurance Programs as of September 30, 2019 (*dollars in thousands*):

	Unaudited	
	FY 2019	*FY 2018*
Premium Base Health Plans		
Full Costs	$ 740,285	$ 663,954
Premiums Collected	(754,719)	(675,142)
Total Net Revenue	**$ (14,434)**	**$ (11,188)**

Premium Base Health Plans consist of several programs with coverage offered to Active Duty, Active Duty Family Member(s), Retirees and Reserve members. The programs include TRICARE CHCBP, TYA, TRS, TRR, Prime and Select which together make up the TRICARE Insurance Portfolio. These programs are required to be budget neutral, meaning that the premiums must match the outlays. Premiums are adjusted either upward, or downward at the end of each year to maintain this neutrality. Increases or decreases in the number of beneficiaries enrolling in the programs would cause minimal effects on program cost or premiums collected. Premium rate calculations are based on the benefit cost from the preceding calendar year. Premiums or enrollment fees are based on the Programs benefit cost which eliminates any inherent risk to third parties including the beneficiary and the Manage Care Support Contractor processing the health care claims and the initial collections on behalf of DHA-CRM.

For Calendar Year (CY) 2019 Monthly Premium Rates are established on an annual basis in accordance with title 10, U.S.C. Section 1076d, e and 1110b along with title 32, Code of Federal Regulations, part 199.24, 25 and 26, as enacted by Section 701 of NDAA for Fiscal Year 2017; Public Law 114 328. The enrollment fee and or premium collections are credited to the DHP appropriation available for the fiscal year collected.

TRS and TRR rates are calculated from enrollment-weighted average annual costs based on the actual cost of benefits provided during the preceding calendar year. Renewal in a specific plan is automatic unless declined. A member, and the dependents of the member, of the Selected Reserve of the Ready Reserve of a reserve component of the armed forces are eligible for health benefits under TRS program. Termination of coverage in TRS is based upon the termination of the member's service in the Selected Reserve. TRR basically follows the same rules of coverage as TRS for members of the Retired Reserve who are qualified for a non-regular retirement but are not yet age 60. Termination of eligibility is upon obtaining other TRICARE Coverage. TYA premium rates are calculated from the Military Health System Data Repository based on enrollees for the previous 24-month period. Dependents under the age of 26 and who are not eligible to enroll in an eligible employer-sponsored plan can enroll in the TYA program. Coverage is terminated once the dependent turns 26 years of age. CHCBP premium rates are calculated from total premiums under Government Employees Health Association (GEHA) Standard plan within the Federal Employee Health Benefit (FEHB) Program. The plan provides temporary health

care coverage for 18 to 36 months when a Service member and/or Family member(s) are no longer entitled to TRICARE. TRICARE Prime and Select premium rates are established on an annual basis in accordance with title 10 U.S.C. 1097a. An enrollment of a covered beneficiary in TRICARE Prime and Select is automatically renewed upon the expiration of the enrollment unless the renewal is declined. The enrollment of a dependent of the member of the uniformed services may be terminated by the member or the dependent at any time. Active duty service members must enroll in Prime. Family members may choose to enroll in Prime or Select.

Beneficiary claims for Premium health care services are processed through TEDS. The liability balance represents unpaid claims received as of the end of the reporting period. The risk for future claim cost are accounted for under the IBNR calculation. The IBNR change is a net result of several factors that increase or decrease the reserve, including change in claims cost and volume per member, changes I administration cost estimates and required margin, change in population size, and movement of health care delivery to alternative types of service.

The table below presents the changes in the liability balance for unpaid insurance claims.

Dollars in Thousands	*Unaudited*	
	FY 2019	***FY 2018***
Beginning Balance	$ 1,744,271	-
Claims Expense	14,170,220	-
Claims Adjustment Expenses	(27,391)	-
Payments to Settle Claims	(13,852,160)	-
Recoveries and Other Adjustments	3,551	
Ending Balance	**$ 2,038,491**	**$ -**

Required Supplementary Stewardship Information

Non-Federal Physical Property

The DHP operates MTFs overseas which require the use of land, buildings, and other overseas facilities. These assets are obtained through various international treaties and agreements negotiated by the Department of State. In order to keep these facilities mission ready, DHP also purchases capital assets with appropriated funds. When these treaties expire, ownership of these purchased assets and any related improvements to these MTFs revert to the host country. DHP acknowledges that this meets the definition of nonfederal physical property but does not currently track or have a process in place to report the required information. As such, DHP acknowledges a departure from SFFAS 8, *Supplementary Stewardship Reporting*.

Research and Development

Military combat is a joint service activity and ensuring the best quality medical care of the warfighter must also be a cross-component effort. The medical mission of the DoD is to enhance DoD and our Nation's security by providing health support for the full range of military operations and sustaining the health of all those entrusted to our care. In order to be responsive to current needs and ready for the next fight, DoD invests significant resources into research and development of medical materiel products (e.g., equipment, tools, and devices) and knowledge products (e.g., clinical practice guidelines and protocols) for the warfighter.

The DHA is a joint, integrated CSA that enables the Army, Navy, and AFMS to provide a medically ready force and ready medical force to CCMDs in both peacetime and wartime. The DHA leads the MHS integrated system of readiness and health to deliver the Quadruple Aim (increased readiness, better health, better care, and lower cost) to MHS beneficiaries and is responsible for driving greater integration of clinical and business processes across the MHS.

Within DHA, the Research and Development Directorate (J-9) leads the discovery, development, and delivery of enhanced pathways to military health and readiness with the vision to bridge the future of military health and readiness. The DHA J-9 research and development activities are presented in the following three major categories:

- ***Basic research***: systematic study to gain knowledge of the fundamental aspects of phenomena and of observable facts without specific applications toward processes or products in mind. It includes all scientific study and experimentation directed toward increasing fundamental knowledge and understanding in those fields of physical, engineering, environmental, and life sciences related to long-term national security needs.
- ***Applied research***: systematic study to understand the means to which a recognized and specific need may be met. It is a systematic expansion and application of knowledge to develop useful material, devices, and systems or methods. It may translate promising basic research into solutions for broadly defined military needs, short of system development.
- ***Development***: systematic use of the knowledge gained from research to produce useful materials, devices, systems, or methods, including the design and development of prototypes and processes. It includes concept and technology demonstrations of components and subsystem or system models; validating component and subsystem maturity prior to integration; and mature system development, integration, and demonstration.

The following are highlights of some of the research and development programs/projects and their accomplishments:

Basic Research

In-House Laboratory Independent Research (ILIR) Program

The ILIR Program at the USUHS is designed to answer fundamental questions of importance to the military medical mission of the DoD in the areas of Combat Casualty Care, Infectious Diseases, Military Operational Medicine, and Chemical, Biological, and Radiologic Defense. Additionally, it facilitates the recruitment and retention of faculty; supports unique research training for military medical students and resident fellows; and allows the University's faculty researchers to collect pilot data towards military relevant medical research projects.

What this program will accomplish:

Infectious Disease

- Generate data and information on immunology and molecular biology of bacterial, viral, and parasitic disease threats to military operations to develop preventive and treatment measures.

Military Operational Medicine

- Map deployment and operational stressors faced by Service Members to further develop management techniques and strategies.
- Determine the effects of dietary and nutritional supplements on military and medical training readiness.

Combat Casualty Care

- Determine the accuracy of traumatic brain injury (TBI) diagnosis in the emergency department (ED) to ensure patients receive appropriate follow-up care, avoid risk of subsequent injury, and are aware of possible long-term consequences.
- Gain increased knowledge in the areas of regenerative medicine, rehabilitation, neurological, limb loss, and pain management to best serve our Service Members.

Basic Operational Medical Research Sciences Program

The Basic Operational Medical Research Sciences Program provides support for basic medical research directed toward greater knowledge and understanding of the fundamental principles of science and medicine that are relevant to the improvement of Force Health Protection. Research in this program is designed to address areas of interest to the Secretary of Defense regarding Wounded Warriors, capabilities identified through the Joint Capabilities Integration and Development System, and sustainment of DoD and multi-agency priority investments in science, technology, research, and development.

What this program will accomplish:

Military Infectious Diseases

- Develop methods to understand the dynamics of microbial communities in infected and healing wounds.
- Prevention, treatment, and management in discovery and development of anti-bacterial agents for biofilms and multi-drug resistant organisms (MDROs) and biomarkers.

Combat Casualty Care

- Model the complexities of trauma to enable future automated and semi-automated decision support algorithms and enable medical and non-medical personnel to rapidly identify, stabilize, and treat casualties with trauma.
- Develop an understanding of trauma-associated pathophysiologic mechanisms using advanced hemostatic and resuscitation approaches in prolonged field care scenarios.

Applied Research

Applied Biomedical Technology Program

The Applied Biomedical Technology Program provides applied research funding to refine concepts and ideas into potential solutions for military health and performance problems, with a view toward evaluating technical feasibility. Research in the Applied Biomedical Technology Program will support efforts such as the Precision Medicine Initiative which seeks to increase the use of big data and interdisciplinary approaches to establish a fundamental understanding of military disease and injury to advance health status assessment, diagnosis, and treatment tailored to individual Service Members and beneficiaries.

What this program will accomplish:

Applied Biomedical Technology

- Optimize the performance and safety in extreme environments by understanding bioenergetic requirements during military diving operations.
- Create systems biology-based approaches to understand combined burn and radiation injuries.
- Research wound infections to develop increased ability to predict infections and better treatment options for infections with MDROs, and development of biomarkers assays for diagnosis of infection.

Combating Antibiotic Resistant Bacteria (CARB)

- Establish sustainable research efforts designed to evaluate viable small molecule candidate antibacterial agents for planned development for the DoD and Public Health benefit.
- Conduct screenings against military relevant strains and biofilms to select compounds for continued development.
- Synthesize specifically designed novel drugs for lead optimization efforts, exploiting established in vivo model standards, and evaluating late stage external programs that could potentially treat military relevant resistant bacteria.

Military HIV Research

- Develop and optimize methods of large-scale production of new vaccine candidates for testing in Africa and Asia, representing the breadth of HIV diversity.
- Evaluate vaccine candidates of interest to assess their capability to induce protective immune responses in non-human primates by using novel diversity systems.
- Optimize a delivery system containing a diverse mixture of antigens for HIV subtypes A, B, C, D, and E and test in non-human primates.
- Identify and develop new clinical trial sites in Europe, Southeast Africa and Asia, and the US that will allow scientists the opportunity to test future vaccine candidates against predominant HIV subtypes circulating in those respective parts of the world.

Medical Technology Program

The Medical Technology Program supports developmental research to investigate new approaches that will lead to advancements in biomedical strategies for preventing, treating, assessing, and predicting the health effects of human exposure to ionizing radiation as well as radiation combined with injuries (burns, wounds, hemorrhage), termed combined injury. Research ranges from exploration of biological processes likely to form the basis of technological solutions to initial feasibility studies of promising solutions.

What this program will accomplish:

Radiation Countermeasures

- Prevent and mitigate the health consequences from exposures to ionizing radiation, in the context of probable threats to US forces in current tactical, humanitarian and counterterrorism mission environments.
- Develop and patent Hematological Acute Radiation Injury (HARI) Index Algorithm for Rapid Early-phase Radiological Triage Applications.
- Test and evaluate promising drug substances and products for radiation countermeasures development for mixed-field radiation exposure and for Radiation-Induced Gastrointestinal Syndrome (GI-ARS) in mice using the Small Animal Radiation Research Platform (SARRP).

Bio dosimetry

- Establish a mouse total-body irradiation model for combined hematological and proteins bio dosimetry approach following the mixed field along with one already established and evaluated for pure proton exposure.
- Evaluate the acute and delayed effects of low-moderate doses of total-body radiation exposure and develop biomarkers to identify the acute and long-term effects of these low-moderate doses radiation injury in mouse model.

Development Research

Medical Products Support and Capabilities Enhancement Activities Program

Medical Products Support and Capabilities Enhancement Activities Program tests, evaluates, and supports the enhancement of existing medical products and medically-related IT systems within the areas of medical simulation, infectious disease, tactical combat casualty care, military operational medicine, and clinical rehabilitative medicine. This is an intramural research program focused on evaluating new commercial medical capabilities suitable for theater; testing fielded capabilities to determine if they can function in an expanded or altered operationally-relevant environment; and investigating the potential to incorporate emerging medical or non-medical technologies into fielded medical systems.

What this program will accomplish:

Medical Products and Capabilities Enhancement Activities

- Design a litter that will work for all ground, rotary winged and fixed winged aircraft used by the DoD.
- Evaluate and down-select laser eye protection that meets US Coast Guard US Navy aviator human performance criteria, demonstrates cockpit compatibility, and which can advise on follow-on flight testing and acquisition decisions. Assess the existing airway management devices used by military medics with the goal of producing evidence-based consensus recommendations to manage airway compromise, the second leading cause of potential preventable death on the battlefield.

Medical Technology and Development Program

The Medical Technology Development Program provides funding for promising candidates solutions that are selected for initial safety and effectiveness testing in animal studies and/or small scale human clinical trials regulated by the US Food and Drug Administration (FDA) prior to licensing for human use.

What this program will accomplish:

Medical Technology Development

- Assessment of rehabilitation outcomes following severe neuromusculoskeletal injuries.
- Technology development activities to stop non-compressible hemorrhage and improve delayed evacuation and prolonged field care paradigms.
- Refine and improve predictive auditory injury models to update acoustic injury standards for health hazard assessment.
- Develop tools to optimize return to duty after lower extremity injury, and head supported mass acute injury predictive models for mounted and dismounted environments.

Medical Products Support and Advanced Concept Development

The Medical Products Support and Advanced Concept Development program provides funding to support advanced concept development of medical products that are regulated by the FDA; clinical and field validation studies supporting the transition of FDA-licensed and unregulated products and medical practice guidelines to the military operational user, prototyping; risk reduction and product transition efforts for medical IT applications such as coordination with the Program Executive Office for possible integration in the MHS; and medical simulation and training system technologies.

Combat Casualty Care

- Development of an FDA approved drug treatment for moderate - severe TBI to improve the ability of brain injured service members to resume normal life activity as much as possible; and minimize hearing loss in Service members within a few days after noise-induced injury.
- Accelerated development of a product to stop massive intracavitary abdominal bleeding that cannot be mitigated by current solutions to temporarily stabilize the patient until the bleeding can be permanently stopped by a surgeon.
- Develop new pharmacotherapeutics to foster recovery of US Service members and Veterans with combat-related posttraumatic stress disorder.
- Develop a solution for earlier identification of patients at risk for shock and possible death due to blood loss.
- Increase Service Member health, readiness and performance through the development of a suite of wearable sensors and algorithms to communicate actionable information to unit leaders.

Research and Development Program Outlays

Program: DHP RDT&E Program *Program Outlays* *(dollars in thousands)*						
Fiscal Year:	**2019-2020**	**2018-2019**	**2017-2018**	**2016-2017**	**2015-2016**	**Total**
Basic Research	$ 404,890	$ 4,594	$ 7,912	$ 7,940	$ 5,546	**$ 430,882**
Applied Research	$ 206,697	$ 43,403	$ 299,153	$ 299,508	$ 1,337,362	**$ 2,186,123**
Development	$ 1,125,985	$ 463,219	$ 712,204	$ 854,492	$ 1,003,324	**$ 4,159,224**
Total	**$ 1,737,572**	**$ 511,216**	**$ 1,019,269**	**$ 1,161,940**	**$ 2,346,232**	**$ 6,776,229**

**Note: Amounts in this table are based on outlays and as such will not agree to DHP's Statements of Net Cost*

Research and Development Program Outcomes and Outputs

Program: DHP RDT&E Program Outcomes and Outputs						
Fiscal Year:	**FY 2019**	**FY2018**	**FY2017**	**FY2016**	**FY2015**	**Total**
Clinical Practice Guideline	0	1	0	0	0	**1**
Programs Transitioned to Advanced Development*	8	12	11	10	15	**56**
Patents/Patent Applications	350	272	277	301	217	**1,417**
Publications	5,535	5,225	4,064	3,907	2,355	**21,086**

**Material Development Decision, or beyond, has signed Technology Transition Agreement with developer, or delivered to a Program Manager.*

Required Supplementary Information

Deferred Maintenance and Repairs

Although DHP receives the economic benefit and is responsible for the sustainment of various general property, plant and equipment, the DHP did not disclose deferred maintenance for FY 2019 in accordance with U.S. GAAP per SFFAS 42, *Deferred Maintenance and Repairs: Amending Statements of Federal Financial Accounting Standards 6, 14, 29, and 32*.

The DHP acknowledges departures from U.S. GAAP related to leases as discussed in Note 1.C., Departures from U.S. GAAP.

Combining Statements of Budgetary Resources for the year ended September 30, 2019 *(dollars in thousands)*	***Operations, Readiness and Support***	***Procurement***	***Research, Development, Test and Evaluation***	***Family Housing and Military Construction***	***Total Budgetary Accounts***
BUDGETARY RESOURCES					
Unobligated balance from prior year budget authority, net	$ 3,358,666	$ 309,652	$ 1,472,237	$ 947,177	$ 6,087,732
Appropriations (discretionary and mandatory)	31,335,216	683,702	1,868,910	487,976	34,375,804
Spending Authority from offsetting collections (discretionary and mandatory)	3,844,261	3,779	47,529	-	3,895,569
TOTAL BUGETARY RESOURCES	**$ 38,538,143**	**$ 997,133**	**$ 3,388,676**	**$ 1,435,153**	**$ 44,359,105**
STATUS OF BUDGETARY RESOURCES					
Total New obligations and upward adjustments	$ 36,843,588	$ 754,864	$ 1,790,318	$ 696,806	$ 40,085,576
Apportioned, unexpired accounts	357,862	200,466	1,525,842	669,273	2,753,443
Exempt from apportionment, unexpired accounts	163,066	-	-	-	163,066
Unapportioned, unexpired accounts	-	-	-	-	-
Unexpired unobligated balance	520,928	200,466	1,525,842	669,273	2,916,509
Expired unobligated balance	1,173,627	41,801	72,518	69,074	1,357,020
Total Unobligated balance, end of year	1,694,555	242,267	1,598,360	738,347	4,273,529
TOTAL STATUS OF BUDGETARY RESOURCES	**$ 38,538,143**	**$ 997,131**	**$ 3,388,678**	**$ 1,435,153**	**$ 44,359,105**
OUTLAYS, NET					
Outlays, Net (discretionary and mandatory)	$ 31,847,368	$ 557,828	$ 1,400,915	$ 570,512	$ 34,376,623
Distributed offsetting receipts	-	-	-	-	-
TOTAL NET OUTLAYS	**$ 31,847,368**	**$ 557,828**	**$ 1,400,915**	**$ 570,512**	**$ 34,376,623**

Combining Statements of Budgetary Resources for the year ended September 30, 2018 (dollars in thousands)	Operations, Readiness and Support	Procurement	Research, Development, Test and Evaluation	Family Housing and Military Construction	Total Budgetary Accounts
BUDGETARY RESOURCES					
Unobligated balance from prior year budget authority, net	$ 3,161,945	$ 365,031	$ 1,319,109	$ 906,525	$ 5,752,610
Appropriations (discretionary and mandatory)	31,803,899	498,350	1,871,866	645,295	34,819,410
Spending Authority from offsetting collections (discretionary and mandatory)	3,510,602	-	19,353	-	3,529,955
TOTAL BUGETARY RESOURCES	**$ 38,476,446**	**$ 863,381**	**$ 3,210,328**	**$ 1,551,820**	**$ 44,101,975**
STATUS OF BUDGETARY RESOURCES					
Total New obligations and upward adjustments	$ 35,821,242	$ 572,738	$ 1,757,424	$ 648,366	$ 38,799,770
Apportioned, unexpired accounts	885,408	242,386	1,389,117	840,419	3,357,330
Exempt from apportionment, unexpired accounts	122,809	-	-	-	122,809
Unapportioned, unexpired accounts	4,799	-	-	-	4,799
Unexpired unobligated balance	1,013,016	242,386	1,389,117	840,419	3,484,938
Expired unobligated balance	1,642,188	48,257	63,787	63,035	1,817,267
Total Unobligated balance, end of year	**$ 2,655,204**	**$ 290,643**	**$ 1,452,904**	**$ 903,454**	**$ 5,302,205**
TOTAL STATUS OF BUDGETARY RESOURCES	**$ 38,476,446**	**$ 863,381**	**$ 3,210,328**	**$ 1,551,820**	**$ 44,101,975**
OUTLAYS, NET					
Outlays, Net (discretionary and mandatory)	$ 30,553,433	$ 427,596	$ 1,335,746	$ 612,326	$ 32,929,101
Distributed offsetting receipts	-	-	(7,811)	-	(7,811)
TOTAL NET OUTLAYS	**$ 30,553,433**	**$ 427,596**	**$ 1,327,935**	**$ 612,326**	**$ 32,921,290**

III. Other Information

Summary of Financial Statement Audit and Management Assurances

Table 1 below provides a summary of Financial Statement Audit.

Table 1: *Summary of Financial Statement Audit*[6]

Summary of Financial Statement Audit						
Audit Opinion	**Disclaimer**					
Restatement	**No**					
Material Weaknesses	**Beginning Balance**	**New**	**Resolved**	**Consolidated**	**Reassessed**	**Ending Balance**
Accounting and Financial Reporting Governance and Entity-Level Controls	1					**1**
Financial Reporting - Compilation	1		-1			**-**
Financial Reporting - Universe of Transaction Reconciliations	1					**1**
Financial Reporting - Defense Departmental Reporting System Adjustments	1					**1**
Fund Balance with Treasury	1					**1**
Medical Revenue and Associated Receivables	1					**1**
General Equipment Existence and Completeness	1					**1**
Valuation of Property, Plant, and Equipment	1					**1**
Real Property	1					**1**
Internal Use Software and IUS In-Development	1					**1**
Operating Materials and Supplies and Stockpile Material	1					**1**
Liabilities and Related Expenses	1					**1**
Monitoring and Reporting of Obligations	-	1				**1**
Information Systems	1					**1**
Total material weaknesses	**13**	**1**	**-1**	**-**	**-**	**13**

[6] The Summary of Financial Statement Audit of material weaknesses are from the Independent Auditor's DHP Report on Internal Controls over Financial Reporting.

Table 2 below provides a summary of management assurances

Table 2: *Summary of Management Assurances*[7]

Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)						
Statement of Assurance	**No Assurance**					
Material Weaknesses	**Beginning Balance**	**New**	**Resolved**	**Consolidated**	**Reassessed**	**Ending Balance**
Accounting and Financial Reporting Governance and Entity-Level Controls	2				-2	-
Financial Reporting - Compilation	1	2	-1			2
Financial Reporting - Universe of Transaction Reconciliations	2	3				5
Financial Reporting - Defense Departmental Reporting System Adjustments	2	1				3
Fund Balance with Treasury	4	6				10
Medical Revenue and Associated Receivables	2	6				8
General Equipment Existence and Completeness		3				3
Valuation of Property, Plant, and Equipment	1	1				2
Real Property	1	1				2
Internal Use Software and IUS In-Development	2	1	-1			2
Operating Materials and Supplies and Stockpile Material	2	3				5
Liabilities and Related Expenses	11	8	-1		-1	17
Monitoring and Reporting of Obligations						-
Information Systems	3				-3	-
Total material weaknesses	**33**	**35**	**-3**	**-**	**-6**	**59**

[7] The total number of material weaknesses and non-Compliances for ICOFR, ICO and internal controls over federal financial management system requirements include both material weaknesses and significant deficiencies.

Effectiveness of Internal Control over Operations (FMFIA § 2)						
Statement of Assurance	No Assurance					
Material Weaknesses	**Beginning Balance**	**New**	**Resolved**	**Consolidated**	**Reassessed**	**Ending Balance**
Fund balance with Treasury	1	1	-			2
General Equipment	0	2				2
Governance Structure and Entity-Level Controls	4	6			-1	9
Information Systems	4	1				5
Liabilities	13	7	-11			9
Total material weaknesses	**22**	**17**	**-11**	**-**	**-1**	**27**

Conformance with Federal Financial Management System Requirements (FMFIA§ 4)						
Statement of Assurance	No Assurance					
Material Weaknesses	**Beginning Balance**	**New**	**Resolved**	**Consolidated**	**Reassessed**	**Ending Balance**
Information Systems	1	**46**	**-2**		**2**	47
Total material weaknesses	**1**	**46**	**-2**	**-**	**2**	**47**

Compliance with Section 803(a) of the Federal Financial Management Improvement Act (FFMIA)		
	Agency	**Auditor**
1. Federal financial management system requirements	Lack of compliance noted	Lack of compliance noted
2. Applicable federal accounting standards	Lack of compliance noted	Lack of compliance noted
3. USSGL at transaction level	Lack of compliance noted	Lack of compliance noted

Management's assessment of FFMIA compliance was completed prior to the results of the FY 2019 financial statement audit. Our auditor has noted the DHP financial management systems did not comply substantially with the Federal financial management system's requirements, applicable Federal accounting standards, or application of the USSGL at the transaction level, because of material weaknesses noted in the Independent Auditor's Report on Internal Control over Financial Reporting. The DHP is in the process of evaluating the FY 2019 audit findings contributing to noncompliance to begin the process of formulating remediation plans necessary to bring the financial managements systems into substantial compliance.

Management Challenges

Per OMB Circular A-136 as it relates to form and content of an AFR, the MHS's IG must, "as required by the Reports Consolidation Act of 2000, include as OI, a statement summarizing what the IG considers to be the most serious management and performance challenges facing the agency and assessing the agency's progress in addressing those challenges." For the reporting purposes of the MHS, the DoD IG on behalf of MHS has reviewed DoD's Top Management Challenges for FY 2019 and determined Challenge 10 *Providing Comprehensive and Cost-Effective Health Care* is applicable challenges to the MHS.

Challenge 1: Providing Comprehensive and Cost-Effective HealthCare

Providing healthcare at a reasonable cost without sacrificing quality is an ongoing challenge for the DoD. The MHS must provide quality healthcare for 9.5 million military beneficiaries, within fiscal constraints, while facing increased user demand and increasing overall healthcare costs. The MHS must also respond and adapt to changing demographics, evolving standards for access and quality, advances in science and medicine, complex payment and cost considerations, rapidly evolving IT capabilities, and fluid patient expectations. The DoD will face challenges related to MHS reform as the DHA takes responsibility this year for the MTFs from the Military Services. In addition, the DoD faces challenges in providing behavioral health services to beneficiaries, including preventing suicides and preventing and treating opioid misuse. At the same time, the DoD needs to integrate medical records with the Department of VA and protect the confidentiality of electronic health records.

The MHS is a global, comprehensive, integrated healthcare system that includes a healthcare delivery, combat medical services, public health activities, medical education and training, and medical research and development. The MHS provides medical care to service members, retirees, and their eligible family members. Direct care is provided at MTFs by military, civilian, and contracted providers and purchased care, provided at commercial locations through the TRICARE program, which is the DoD's health care program. The DHA manages the TRICARE program under the authority of the ASD(HA).

The DoD OIG has performed audits and evaluations and issued recommendations covering many different areas of DoD healthcare, including reviews of quality and access to care and cost control, and issued numerous recommendations for improvement. Overall, the DoD has reduced the number of open recommendations related to healthcare and morale issues in the past year, from 114 open recommendations in March 2017 to 96 as of March 31, 2018.

For example, the DoD has implemented recommendations related to a February 2018 evaluation report by the DoD OIG on the MHS Review on quality of care. Specifically, the DoD improved performance at MTFs identified as outliers for three quality of care measures, developed common quality policy for the Military Services, and used a performance management system to improve quality of care as directed by the Secretary of Defense.

However, recommendations from other DoD OIG reports remain open, such as recommendations to pursue collections on improper payments to TRICARE healthcare providers and on delinquent medical debts, and recommendations for establishing a multidisciplinary approach for obtaining the data necessary to make comprehensive DoD Suicide Event Report submissions.

DoD MHS Reform

The required transfer of responsibility for the MTFs from the Military Services to the DHA will be challenging for the DoD. Historically, the Services managed and operated the MTFs. The FY 2017 NDAA mandated that by October 1, 2018, a single agency, the DHA, would be responsible for the administration of all MTFs.

According to the Under Secretary of Defense for Personnel and Readiness (USD (P&R), the optimal end state is that under the direction of the DHA, the MHS should be a fully integrated system of readiness and healthcare delivery. The DHA will therefore have direct control over MTFs, while the Military Services will retain control over their medical uniformed personnel and certain non-healthcare delivery functions, such as medical readiness.

According to the USD (P&R), substantial challenges remain in implementing such a major reform, such as maintaining a ready medical force and a medically ready force. Transitioning over 457 MTFs worldwide to DHA authority, direction, and control by October 1, 2021, will be difficult.

Establishing authority, direction, and control over MTFs healthcare must be carefully planned to make sure that clear authorities over Service medical personnel are properly established. For example, a May 2018 report by the DoD OIG determined that three Air Force MTFs did not meet beneficiary demand for appointments because the Air Force Surgeon General did not have the authority to direct Air Force medical personnel in the MTFs. It is imperative that the DHA has clear authority, direction, and control over each MTFs to be able to hold facility commanders accountable for providing appropriate medical care.

Behavioral Health

Identifying and providing care for behavioral health problems, such as suicides and opioid misuse, is a critical challenge for the DoD. Diagnosed mental health disorders in the total population of active duty personnel increased by 6 percent from 2005 to 2016.

Between 2012 and 2016, mental disorders were among the leading cause for hospitalization of active duty service members, accounting for between 12 to 15 percent of hospitalizations during those years. In 2017, the DoD reported that mental health disorders accounted for more hospital bed days than any other morbidity category among the active military components. In addition, mental health disorders accounted for the second most common reason for outpatient clinic visits by active duty service members in 2016.

Suicide Prevention

Substance abuse, including opioids abuse, remains a significant readiness concern for the DoD, particularly due to its relationship with suicide. A recent Medical Surveillance Monthly Report study found that service members taking a combination of narcotics, antidepressants, and sedative medications have an increased risk for suicidal thoughts.

Preventing suicides by DoD military personnel remains a challenge for the DoD. The DoD responded to a rise in active duty suicide deaths from 2008 to 2011 by establishing the Defense Suicide Prevention Office. This office works with the Military Services to implement suicide prevention programs, to publish related policies, and to ensure that certain populations at high risk, such as transitioning service members, have access to quality mental healthcare and suicide prevention resources. In November 2017, the DoD issued DoD Instruction 6490.16, “Defense Suicide Prevention Program.” The Instruction outlines processes for planning, directing, guiding, and resourcing to effectively develop and integrate the Suicide Prevention Program within the DoD.

Despite these efforts, the average suicide rate, across all Military Services, has remained consistent since 2013. The most recent DoD Suicide Event Report (in 2016) shows the suicide mortality rate was 21.1 deaths per every 100,000 active duty service members. The 2016 suicide mortality rate for the Reserves, combined across all Military Services and regardless of duty status, was 22.0 deaths per 100,000 reservists. The 2016 suicide mortality rate for the National Guard, combined

across the Air and Army Guard and regardless of duty status, was 27.3 deaths per 100,000 members of the Guard population. However, it is important to note that these rates are similar to the suicide mortality rate of the U.S. general population, after accounting for differences in the age and sex distributions between the U.S. general population and the military populations. The FY 2015 NDAA expanded the DoD's collection of suicide data to include military family members. The DoD is now required to collect, report, and assess data regarding military family suicide. However, the current tracking systems, which are dependent on voluntary action by service members, provide incomplete mortality counts for suicides of military family members.

In November 2014, the DoD OIG recommended that the USD (P&R) publish guidance requiring suicide event boards to establish a multidisciplinary approach for obtaining the data necessary to make comprehensive DoD Suicide Event Report submissions. Additionally, the DoD OIG recommended that the USD (P&R) create systems to enable military leaders to develop installation level command suicide event tracking reports. However, the recommendation remains open. Without a comprehensive and complete DoD Suicide Event Report submission, it will be difficult for the DoD to conduct the trend or causal analysis necessary to develop effective suicide prevention policy and programs.

Opioid Misuse and Treatment

The DoD also faces challenges in identifying and treating those DoD beneficiaries who are misusing opioids. Opioids are a class of drugs that include heroin, synthetic opioids such as fentanyl, and pain relievers available legally by prescription, such as oxycodone, hydrocodone, codeine, morphine, and many others.

The DoD must ensure that military healthcare providers prescribe opioids only to those patients who need them and adhere to guidelines that reduce the chance of addiction. Providers often receive pressure from patients to provide opioids to treat pain when the opioid prescriptions may be putting the patients at risk for addiction. As a result, alternate pain relief therapies may be better long-term options for those patients. The DoD healthcare system must also be aggressive in identifying those patients who are addicted to opioids and provide treatment plans for them. The DHA Director stated in June 2018 that the DoD is "making headway, but there is more to be done in educating our patients and providers on threats from opioid addiction and strategies to reduce abuse."

The DoD OIG is conducting several reviews related to opioid abuse. For example, the DoD OIG is auditing whether beneficiaries were overprescribed opioids at selected MTFs.

The DoD OIG is also evaluating the DoD's management of opioid use disorder treatment, including whether the DoD has developed policies and programs to manage the treatment of opioid use disorder, identified and resolved barriers to opioid use disorder treatment, and established and implemented measures to improve opioid use disorder treatment.

The Defense Criminal Investigative Service (DCIS), the criminal investigative arm of the DoD OIG, also conducts investigations related to opioid misuse. For example, DCIS investigated allegations that a Florida pain clinic physician illegally distributed controlled substance, including opioids and sleeping medication, from the clinic. The physician overprescribed these medications to several patients, including TRICARE beneficiaries, with no standard of care or medical necessity involved. The case resulted in the conviction of the physician and one other clinic employee for unlawful distribution of a controlled substance. Two additional clinic employees were convicted of conspiracy to distribute a controlled substance.

Additionally, DCIS investigated allegations that a physician was prescribing medically unnecessary opioid medication to his patients, including military members and their dependents. This investigation revealed a scheme between the physician, hired patient recruiters, and select patients to fraudulently prescribe opioids and then bill Government health benefit programs, including TRICARE, for the medications and associated examinations. The case resulted in the physician being convicted of multiple counts of structuring currency transactions.

Increasing Healthcare Costs

The DoD also must confront the challenges of containing healthcare costs and preventing healthcare fraud. Healthcare costs in the US have grown dramatically, and MHS costs have been no exception. The DoD FY 2017 appropriations for healthcare were $33.5 billion, almost triple the FY 2001 appropriation of $12.1 billion. The DoD was appropriated $31.0 billion for the DHP in FY 2019.

As previously stated Management's Discussion and Analysis, the rise in healthcare costs to the DoD is commensurate with the civilian employers in the United States. The MHS in recent years has managed to slow the accelerating rate of health costs with greater centralization of processes and decision-making, including more robust enterprise-supporting shared services. Health care cost containment is a priority for the Department. However, MHS activities are inextricably linked to the civilian health care market.

Healthcare Fraud

One of the leading contributors to increasing healthcare costs is fraud. Healthcare fraud continues to be one of the top investigative priorities for DCIS. As of July 2018, DCIS had 510 open healthcare investigations. In FY 2017 and FY 2018 combined, DCIS health care fraud investigations resulted in 212 criminal charges and 113 convictions, the seizure of $31 million in assets, and $138 million in recoveries for TRICARE and the DHA.

However, health care fraud schemes constantly evolve. As one vulnerability is addressed, corrupt individuals look for other vulnerabilities within the healthcare payment system to exploit. The DoD needs to be constantly vigilant to identify healthcare fraud schemes and ensure internal controls are in place to prevent fraudulent payments.

The DoD OIG has identified several categories of healthcare payments susceptible to fraud, including compound drugs and treatment for autism.

Compound Drugs

The DoD OIG continues to investigate fraud arising from the compound drug schemes that defrauded TRICARE in 2014 and 2015, before the DHA changed its reimbursement policies for compound drugs. Compound drugs are developed from combining, mixing, or altering two or more ingredients to create a customized medication for an individual patient. Compound drug fraud schemes involved providers who prescribed compound drugs, including various pain and other creams, without examining or even meeting the patient; medication refills sent without the consent of the patient; kickbacks paid to providers, marketers, and patients; and grossly inflated bills for prescriptions. These schemes took advantage of a TRICARE reimbursement policy that allowed for full and immediate reimbursement of prescribed compound drugs.

For example, one compounding pharmacy and associated laboratory in Texas sought reimbursement for compounding pharmaceutical prescriptions that were not medically necessary, never received by the patient, and prescribed by physicians who had never actually examined nor had even seen the recipients of the medications. Service members were involved in the scheme by agreeing to accept kickbacks in exchange for the use of their personal identifying information to be used to facilitate additional billings to the DHA for compound prescriptions. In this case, four individuals have been convicted of various crimes, $4.8 million is anticipated to be ordered back to the DHA as restitution, and over $1 million in assets have been seized.

The DHA eventually responded to rapidly increasing costs for compound drugs. In 2015, it changed its reimbursement policy for compound drugs in response to the significant fraud that occurred in 2014 and 2015. The change in policy reduced the DHA's monthly costs for compound drugs from $497 million in April 2015 to $10 million in June 2015. As compared to payments for compound drugs of $1.6 billion in FY 2015, the DoD paid only $10.1 million for compound drugs for the entire FY 2017, demonstrating the dramatic effect of the changes in the reimbursement policy.

However, fraud and escalating costs can also occur in non-compound pharmaceuticals. A DoD OIG audit in November 2017 reported that the DHA often took more than 6 months to implement new cost controls for drugs. The DoD OIG recommended that the DHA implement procedures allowing expedited placement of controls to limit rapidly rising drug costs, and the DHA took actions to implement the recommendation.

Fraudulent and Unsupported Claims for Autism Treatment

The DoD OIG has also identified significant fraudulent activity and improper payments for Applied Behavioral Analysis services, which employs techniques and principles to encourage a meaningful and positive change in behavior. Applied Behavioral Analysis is a benefit offered by TRICARE for children with a diagnosis on the Autism Spectrum.

In a March 2018 audit report, the DoD OIG projected that the DHA improperly paid $81.2 million of the total $120.1 million paid to Applied Behavioral Analysis companies in the TRICARE North Region for services provided in 2015 and 2016. The audit determined that documentation was insufficient to support the payments because the providers or companies did not provide supporting documentation or did not provide adequate details in the documentation to support their claims.

The DCIS has also conducted investigations to address fraud within Applied Behavioral Analysis therapy and autism treatment. For example, one DCIS case occurring in South Carolina resulted in a provider company repaying the U.S. Government $8.8 million. The payment was made to resolve allegations that this company billed TRICARE and other Government programs for Applied Behavioral Analysis therapy services provided to children with autism in which the company either misrepresented the services provided or did not provide the services at all.

However, as the DHA continues to make progress in controlling costs and tightening internal controls in certain areas, those intent on committing fraud seek other vulnerabilities to exploit. Emerging areas of concern for fraud within the DoD health care system involve genetic and DNA testing, vaccinations, durable medical equipment (DME), and opioids. The DHA needs to regularly and comprehensively review billing trends to look for the next fraud schemes and implement effective controls to help prevent payments for fraudulent claims.

Payments for Services with Limited or No Cost Controls

The DHA also pays for some services and products with limited or no cost containment controls. Cost containment controls could include establishing maximum allowable rates and obtaining authorizations prior to receiving the services or products. In an April 2018 report, the DoD OIG projected that the DHA overpaid for breast pumps and parts by $16.2 million in 2016 because it had not used negotiated rates or set maximum allowable rates. For example, the DHA paid $1,360 for a breast pump in Alaska while a local large retail store sold the same model for $221. Also, the DHA paid more than the highest rate of Medicaid agencies for approximately 57 percent of breast pump replacement parts, including paying $138 for a single bottle, which was over 20 times the highest Medicaid reimbursement rate of $6.62. The DoD OIG began an audit in March 2018 to review other items that may not have cost containment controls, such as vaccinations and birth control devices.

Collections

In addition, the DoD could better control healthcare costs by proactively collecting for services provided at MTFs. Collections from beneficiaries, insurance companies, and other Government organizations can provide additional funds to the MTFs to be used to help improve access and quality of care through additional doctors or new equipment.

For example, the DoD OIG issued six reports from August 2014 through January 2017 related to collections from non-DoD beneficiaries, which concluded that MTFs did not actively pursue collections from non- DoD beneficiaries for 129 accounts, valued at $13.1 million, of the 145 accounts the DoD OIG reviewed. The DoD OIG is performing follow up work on those six reports and reviewing reimbursements for healthcare provided to VA patients and collections from insurance providers.

Electronic Health Records

The security of electronic health records and integration of those records with the VA also is an important challenge for the DoD. Electronic health records can contribute to improved quality of care, more efficient care, and more convenient care. These records contain sensitive medical history and information about a patient's health, including symptoms, diagnosis, medications, lab results, vital signs, immunizations, and reports from diagnostic tests, and their disclosure could have serious consequences. The security and availability of those records is critical to the patients' privacy and to healthcare providers' ability to treat the patients.

Security of Patient Health Information

According to a report from the Identify Theft Resource Center, a non-profit organization that supports victims of identity theft and educates the public about identity theft, data breaches, cyber security, fraud, and privacy issues, there were 1,579 data breaches in 2017 from business, health and medical, financial, education, and Government and military institutions, exposing more than 179 million records. According to another report from the health compliance analytics company Protenus, over 5.5 million patient records were breached in 2017 across the US. According to a July 2018 article by the HIPAA Journal, the average cost of a data breach in the US is $7.91 million, and healthcare data breaches represent the highest costs for breaches at an average of $408 per record.

These risks affect the DoD also. For example, the DoD OIG identified in 2017 that the DHA and Army officials did not consistently implement effective security protocols to protect systems that stored, processed, and transmitted electronic health records and electronic patient health information. Specifically, DHA and Army officials did not enforce the use of Common Access Cards to access five electronic health record systems and did not comply with DoD password complexity requirements for three systems. In addition, the DoD OIG reported that system and network administrators at three Army facilities did not consistently mitigate known vulnerabilities affecting Army networks, protect stored data for five systems, and grant user access to the seven systems based on the user's assigned duties.

A May 2018 DoD OIG audit had similar findings for the Navy and Air Force electronic health records at five facilities. In addition to many of the problems noted in the DoD OIG report on the Army, the DoD OIG audit reported that system and network administrators did not properly configure electronic health record systems to lock after 15 minutes of inactivity and did not consistently review system activity reports to identify unusual or suspicious activities and access. In short, the DoD needs to ensure adequate controls exist on its healthcare systems to reduce the risk of compromising DoD patients' sensitive healthcare information.

Integration with the Department of Veterans Affairs

The DoD and VA have experienced significant problems in attempting to integrate their respective electronic health records since 1998.

The FY 2017 NDAA directed the DoD and the VA to integrate their electronic health records and gave the departments 5 years to meet this requirement. The Secretary of the VA announced in 2017 that the Department of VA would acquire the same system as the DoD. In May 2018, the VA established a $10 billion contract to overhaul its electronic health records system to make it compatible with the DoD's records.

In FY 2019, the DoD OIG plans to review the DoD and the Department of VA electronic health care systems to determine whether they allow for full interoperability of health care information between DoD, VA, and private sector health care systems.

In summary, providing comprehensive and cost-effective healthcare to the DoD's 9.5 million beneficiaries will continue to be a significant challenge for the DoD. The DoD must carefully plan the transfer of authority, direction, and control of the MTFs to the DHA. The DoD must also continue to seek efficiencies to control costs without undermining timely access to quality healthcare, which is not an easy task. At the same time, the DoD needs to address behavioral disorders and aggressively seek to reduce the number of suicides within the military while also identifying and treating patients suffering from opioid addiction. Finally, the DoD must protect patient health information within its electronic health records and work with the VA to integrate electronic health records between the departments.

Payment Integrity

In accordance with the Improper Payments Information Act of 2002, as amended (31 U.S.C.3321 note), and Appendix B of the OMB Bulletin No. 19-03, "Audit Requirements for Federal Financial Statements," dated August 27, 2019, DoD reports payment integrity information (i.e. improper payments) at the agency-side level in the consolidated DoD AFR. For detailed reporting on DoD payment integrity, refer to the Other Information section of the consolidated DoD AFR at: https://comptroller.defense.gov/ODCFO/afr2019.aspx.

Fraud Reduction Report

OMB Circular No. A-136 requires that, "Under the Fraud Reduction and Data Analytics Act of 2015, each agency must include in its AFR or Performance and Accountability Reports a report on its fraud reduction efforts undertaken in FY 2019." The DHA OIG began working towards its goal of preventing fraud, waste, and abuse a little over three years ago. Prior to the DHA IG's arrival in April 2016, the DHP did not have an IG – it relied on the services and the DoD IG to provide a hotline program and other IG services. The DHA OIG currently has seven civilian government employees and three contract support personnel. During FY 2019, the DHA OIG began transitioning to implementing Congressional direction for reform of the MHS. Under this mandate, the DHA OIG will increase to 54 government personnel to support the entire MHS system and operationalize the four major IG functions of inspection, investigations, teach and train, and assistance. The office is continuing to evolve from a reactive to proactive model by focusing concerted effort in helping the DHP identify and address problems through inspections before occurrence, promoting organizational health, and enabling DHP readiness. In FY 2019, the DHA OIG also took over the external audit program, which includes audits from the DoD IG and Government Accountability Office (GAO).

The DHA OIG derives its authority to inspect and investigate from the Director, DHA. The DHA OIG control and reporting relationship may not be further delegated. Approval with written authority must be gained from the director to conduct inspections or full investigations. However, the DHA OIG can respond to requests for assistance and can conduct informal inquiries, generally to gather initial facts to determine if a formal investigation is warranted, without the Director's personal approval.

In accordance with the authority in DoD Directive 5106.01, the DHA OIG maintains the DHP Hotline Program, ensuring that inquiries resulting from allegations are conducted in accordance with applicable laws, DoD regulations, and policies. Per DoD Instruction (DoDI) 7050.01, the DHP Hotline Program provides a confidential, reliable means for individuals to report fraud, waste and abuse; violations of law, rule or regulation; mismanagement; and classified information leaks involving the DHP. The detection and prevention of threats and danger to the public health and safety of the DoD and the US are essential elements of the hotline mission. The DHP Hotline Program maintains a public awareness campaign ensuring that the current DoD fraud, waste, and abuse hotline poster, prepared by the DoD OIG, is displayed in common work areas. In accordance with DoD Instruction 7600.10 and DoD Instruction 7650.02, the DHA OIG coordinates the external audit program and ensures the effective execution of the audit follow-up program. Audits, evaluations, and investigations contain recommendations to improve program management and operations, and to address fraud, abuse, mismanagement, and waste of DoD funds.

Allegations of Fraud

Hotline personnel promptly report all allegations of fraud to the appropriate Defense Criminal Investigative Organization in accordance with DoDI 5505.02, *Criminal Investigations of Fraud Offenses*, August 29, 2013, as amended. Fraud is defined by DoD regulations as any intentional deception designed to deprive the US unlawfully of something of value or to secure from the US a benefit, privilege, allowance, or consideration to which a person or entity is not entitled. Such practices include, but are not limited to:

- Offering to make a payment or accepting bribes or gratuities
- Making false statements
- Submitting false claims
- Using false weights or measures
- Evading or corrupting inspectors or other officials
- Deceiving either by suppressing the truth or misrepresenting material fact
- Adulterating or substituting materials
- Falsifying records and books of accounts
- Arranging for secret profits, kickbacks, or commissions
- Conspiracy to do any of the above

Audit liaison personnel monitors follow-up responses to all external audits in the accordance with DoDI 7650.03, Follow-up on GAO, DoD IG, and Internal Audit Reports, December 18, 2014.

Performance Metrics and Trend Analysis

Hotline personnel collect and analyze data to:

- Identify opportunities to improve the management of hotline complaints from receipt to resolution
- Identify trends that will help DHP decision-makers combat fraud, waste, abuse, and mismanagement in DHP programs and operations more effectively

Audit liaison personnel coordinates with the appropriate MHS staff to take corrective action on agreed-upon IG DoD and GAO findings and recommendations requiring their action.

Preventing and Deterring Fraud

Curbing fraud is vital to conserving scarce healthcare resources and protecting beneficiaries. Fraud schemes shift over time, but certain healthcare services have been consistent targets. They include services provided by DME suppliers, pharmacy companies, and providers. To secure the future of healthcare for our beneficiaries, the DHP must be vigilant in reducing wasteful spending and promoting better health outcomes at lower costs. During FY 2019, the DHA OIG worked with the DoD IG to close 20 audit recommendations. A review of possible fraud was done concerning DoDIG Audit 2017-084, *"The DHA Improperly Paid for Autism Related Services to Select Companies in the TRICARE South Region,"* DoD IG Audit 2018-084, *"TRICARE North Region Payments for Applied Behavior Analysis Services for the Treatment of Autism Spectrum Disorder,"* and DoD IG Audit 2018-108, *"TRICARE Payments for Standard Electric Breast Pumps and Replacement Parts."* The DHA OIG coordinated with offices to include DHP PI and the appropriate Defense Criminal Investigative Organization, ensuring cost savings were recognized.

DHA OIG will ensure the workforce and culture continue to serve as a reflection of core Department values – values that are rooted in the belief of doing the right thing.

IV. Appendices

Appendix A: Abbreviations & Acronyms

ACGME	Accreditation Council for Graduate Medical Education
ADA	Anti-deficiency Act
ADDP	Active Duty Dental Program
ADP	Additional Discount Program
ADSM	Active Duty Service Members
AEAN	Aggregate Entry Age Normal
AFMS	U.S. Air Force Medical Service
AFR	Agency Financial Report
AHCC	Annual Health Care Cost
AIMS	Accounting and Inventory Management System
AL	Actuarial Liability
ALC	Agency Location Code
ARRA	American Recovery and Reinvestment Act
ASD(HA)	Assistant Secretary of Defense (Health Affairs)
BS	Balance Sheet
BUMED	Navy Bureau of Medicine and Surgery
CAP	Corrective Action Plan
CAP	College of American Pathologists
CCMD	Combatant Command
CCS	Choctaw Contracting Services
CDRL	Contract Data Requirements List
CERCLA	Comprehensive Environmental Response, Compensation, and Liability Act
CFO	Chief Financial Officer
CFR	Code of Federal Regulations
CHAMPUS	Civilian Health and Medical Program of the Uniformed Services
CHCBP	Continued Health Care Benefits Program
CIP	Construction in Progress
CLRS	CFO Load Reconciliation System
CMAC	CHAMPUS Maximum Allowable Charge
CMR	Combat Mission Requirement
CONUS	Continental United States
COR	Contracting Officer Representative
COTS	Commercial Off-the-Shelf
CPI	Consumer Price Index
CPT 4	Current Procedural Terminology
CRM	Contract Resource Management
CSA	Combat Support Agency
CY	Calendar Year
DATA Act	Digital Accountability and Transparency Act of 2014
DCIA	Debt Collection Improvement Act of 1996
DCIS	Defense Criminal Investigative Service
DCPS	Defense Civilian Personnel System
DCS	Duplicate Claims System
DEERS	Defense Enrollment Eligibility Reporting System
DFAS	Defense Finance and Accounting Service
DHA	Defense Health Agency
DHP	Defense Health Program
DISA OKC	Defense Information Systems Agency-Oklahoma City
DLA	Defense Logistics Agency
DMDC	Defense Manpower Data Center
DME	Durable Medical Equipment
DMLSS	Defense Medical Logistics Standard Support
DoD	Department of Defense
DoDI	Department of Defense Instruction
DOL	Department of Labor
DON	Department of Navy
DP	Designed Providers
DPP	Designated Providers Program
DRRS	Defense Readiness Reporting System
DRG	Diagnosis Related Group
ECS	E-Commerce System
EHR	Electronic Health Record
EIC	External Independent Contractors
EIN	Employer Identification Number
EPLS	Excluded Parties List System
ESA	Enterprise Support Activities
ESI	Express Scripts
ESRD	End-stage renal disease
FAD	Funding Authorization Document
FASAB	Federal Accounting Standards Advisory Board
FBCH	Fort Belvoir Community Hospital
FBwT	Fund Balance with Treasury
FCA	False Claims Act
FCP	Federal Ceiling Price

FFATA	Federal Funding Accountability and Transparency Act of 2006
FFMIA	Federal Financial Management Improvement Act
FFS	Federal Financial System
FGB	GFEBS Functional Governance Board
FIAR	Financial Improvement and Audit Readiness
FLSA	Fair Labor Standards Act
FMR	Financial Management Regulation
FSIO	Financial Systems Integration Office
FSRE	Financial Statement Reporting Entity
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
GFEBS	General Funds Enterprise Business System
GMRA	Government Management Reform Act
GONE	Grants Oversight and New Efficiency
GPRAMA	Government Performance and Results Modernization Act of 2010
HA	Health Affairs
HGB	Humana Government Business Inc.
HMO	Health Maintenance Organization
HNFS	Health Net Federal Services
HRO	High Reliability Organization
HRQOL	Health Related Quality of Life
IBNR	Incurred but not reported
ICO	Internal Controls Over Operations
ICOFR	Internal Controls Over Financial Reporting
ICOFS	Internal Controls Over the Financial Systems
IG	Inspector General
ILIR	In-House Laboratory Independent Research
IP	Improper Payment
IPERA	Improper Payments Elimination and Recovery Act of 2010
IPERIA	Improper Payments Elimination and Recovery Improvement Act of 2012
IPIA	Improper Payments Information Act of 2002
iRAPT	Invoice Receipt, Acceptance and Property Transfer
IT	Information Technology
JPC	Joint Pathology Center
JFMIP	Joint Financial Management Improvement Program
LEIE	List of Excluded Individuals/Entities
KSA	Knowledge, Skills and Abilities

LES	Leave and Earnings Statement
M2	MHS Mart
MCSCs	Managed Care Support Contractors
MDR	Military Health System (DHP) Data Repository
MEDCOM	U.S. Army Medical Command
MERHCF	Medicare-Eligible Retiree Health Care Fund
MHBs	Military Health Benefits
MHS	Military Health System
MILCON	Military Construction
MTF	Military Treatment Facility
NWCF	Navy Working Capital Fund
NCR	National Capital Region
NCR MD	National Capital Region Medical Directorate
NDAA	National Defense Authorization Act
NGPL	No Government Pay List
NIPRNET	Internet/Non-secure Internet Protocol Router Network
NOAA	National Oceanic & Atmospheric Administration
O&M	Operation and Maintenance
OACT	Office of the Actuary
OASD(HA)	The Office of the Assistant Secretary of Defense for Health Affairs
OCONUS	Outside of the Continental United States
OFF	Oracle Federal Financials
OGC	Offices of General Counsel
OHI	Other Health Insurance
OI	Other Information
OMB	Office of Management and Budget
OPM	Office of Personnel Management
OP	Other Procurement
OP	Overpayment
OSD	Office of the Secretary of Defense
OUSD C	Office of the Under Secretary of Defense (Comptroller)
PCM	Primary Care Manager
PHS	Public Health Service
PI	Program Integrity
PIMS	Participant Information Management System
POG	Process Owner's Group
POS	Point-of-service
PPA	Prompt Payment Act
PPO	Preferred Provider Organization

PVFB	Present Value of Future Benefits
PVFNC	Present Value of Future Normal Costs
PTSD	Post-Traumatic Stress Disorder
QA	Quality Assurance
RCRA	Resource Conservation and Recovery Act
RDT&E	Research Development Test & Evaluation
ROI	Return on Investment
SARA	Superfund Amendments and Reauthorization Act
SBR	Statement of Budgetary Resources
SDP	Savings Deposit Program
SDP	Standard Discount Program
SFFAS	Statement of Federal Financial Accounting Standards
S/L	Straight Line
SMA	Service Medical Activity
SME	Subject Matter Expert
SMS	Sustainment Management System
SNC	Statement of Net Cost
SNP	Statement of Changes in Net Position
SOFA	Status of Forces Agreement
SSN	Social Security Number
TAMP	Transitional Assistance Management Program
TBI	Traumatic Brain Injury
TCM	TRICARE Claims Management
TDEFIC	TRICARE Dual Eligible Fiscal Intermediary Contract
TDP	TRICARE Dental Program
TEDS	TRICARE Encounter Data Set
TFL	TRICARE for Life

TFM	Treasury Financial Manual
tIMO	Transitional Intermediate Management Organization
TMA	TRICARE Management Activity
TMOP	TRICARE Mail Order Pharmacy
TNC	Treasury Nominal Coupon Issues
TOM	TRICARE Operations Manual
TOP	TRICARE Overseas Program
TOP	Treasury Offset Program
TPharm	TRICARE Pharmacy Program
TPR	TRICARE Prime Remote
TPRADFM	TRICARE Prime Remote for Active Duty Family Members
TRDP	TRICARE Retiree Dental Program
TRO	TRICARE Regional Offices
TSCA	Toxic Substances Control Act
TSM	TRICARE Systems Manual
TYA	TRICARE Young Adult Program
UHM&VS	United Health Military and Veterans Services
UP	Underpayment
USACE	United States Army Corps of Engineers
U.S.C.	United States Code
USFHP	Uniformed Services Family Health Plan
USSGL	U.S. Standard General Ledger
USUHS	Uniformed Services University of the Health Sciences
VA	Veterans Affairs
WIC	Women, Infant, and Children
WPS	Wisconsin Physicians Services
WRNMMC	Walter Reed National Military Medical Center

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