

	Agency	Auditor
Overall Substantial Compliance	No	No
1. System Requirements	No	No
2. Accounting Standards	No	No
3. U.S. Standard General Ledger at Transaction Level	No	No

**✓CHECK IT**

The Department of Defense leadership is keenly aware and actively involved in helping its managers and employees understand that effective internal management controls are important to getting the job done right. The Department reminds its personnel that the Defense mission cannot be accomplished by the warfighters alone; everyone has a job to do, and every job is important. Internal management controls help ensure that what should happen does happen on a daily basis, but first internal management controls must be in place, effective and used. To help draw the attention of the approximately 2.9 million employees in more than 140 countries, the Deputy Secretary of Defense kicked off an awareness campaign known as, the Check It Campaign. The slogan states, “Check It. What gets checked, gets done.”

Details about the campaign may be found at [http://www.defenselink.mil/comptroller/micp/03\\_check\\_it\\_campaign/index.html](http://www.defenselink.mil/comptroller/micp/03_check_it_campaign/index.html)

**Improper Payments Information Act Reporting**

The Improper Payments Information Act (IPIA) of 2002, as implemented by the OMB Circular A-123, Appendix C, “Requirements for Effective Measurement and Remediation of Improper Payments,” requires federal agencies to review all programs and activities annually and identify those that may be susceptible to significant erroneous payments. The Department’s FY 2007 review did not identify any programs or activities at risk of significant erroneous payments in accordance with OMB criteria (programs with erroneous payments exceeding both \$10 million and 2.5% of program payments). However, based on the large volume of transactions or high dollar amounts, the following five programs are reportable in FY 2007: (1) Military Health Benefits, (2) Military Pay, (3) Civilian Pay, (4) Military Retirement, and (5) Travel Pay. Improper payment estimates for these programs are presented in the table below. Additionally, Commercial Pay information is included in Section V, Recovery Audit.

**FY 2007 Estimated Improper Payments**  
(dollars in millions)

<b>Program</b>	<b>Estimated \$</b>	<b>Estimated %</b>
Military Health Benefits	\$ 156	2.00 %
Military Pay	\$ 370	0.51 %
Civilian Pay	\$ 75	0.26 %
Military Retirement	\$ 49	0.13 %
Travel Pay	\$ 44	1.00 %

**I. Risk Assessment**

The Department’s risk assessments for each of the programs identified above addressed the effectiveness of internal

controls in place to prevent improper payments (such as prepayment reviews) as well system weaknesses identified internally or by outside audit activities. While the Department’s improper payment percentages are extremely low, numerous pre- and post-payment controls further minimize and eliminate improper payments. The following paragraphs summarize the processes in place and the results of survey assessment reviews.

**II. Statistical Sampling Process**

The Department uses random sampling methods designed to meet or exceed the OMB requirement of annual estimates of improper payments with a 90% confidence interval (plus or minus 2.5%). Details on these sampling processes can be found at <http://www.defenselink.mil/comptroller/afr/fy2007/FY07AFRSection3IPIA.pdf>.

**III. Corrective Action Plans**

(1) Military Health Benefits. The Department’s contracts have had payment performance standards for military health benefit claims processing in place for many years. Overpayments found in the audit process are projected to the audit universe, and the managed care support contractor is liable for the total amount. This contractual design, combined with numerous prepayment and post-payment controls which effectively minimize improper payments, helps to ensure the Government is not at risk for improper payments in military health benefit payments. Additional discussion of these controls can be found at <http://www.defenselink.mil/comptroller/afr/fy2007/FY07AFRSection3IPIA.pdf>.

(2) Military Pay. Reviews of military pay accounts for FY 2007 resulted in projected improper payments of an estimated \$292 million (.4% of approximately \$73 billion in total military net pay). The majority (approximately \$271 million) are attributable to the Reserve and Guard Components, due to inaccurate and untimely reporting of entitlement data to the automated pay system. The two most significant reporting discrepancies involve leave accountability (Lump Sum Leave payments) and Basic Allowance for Housing. A special review and subsequent data extract of Active Duty in-service collections performed at the recommendation of the IG revealed approximately \$78 million in additional improper payments. Therefore, the total improper payment estimate for military pay, including Active Duty collections and adjusting sample results to preclude over-estimation, is approximately \$370 million (.51%) of net pay.

The Department has worked closely with the Active Duty Components to develop metrics and track timeliness and accuracy of pay entitlements. Senior leaders participate in regular Pay and Personnel Council meetings to discuss problem areas and seek solutions to mitigate discrepancies causing improper payments. This partnership with the Active Duty Components has improved pay entitlement timeliness and accuracy. The Department is developing Reserve and Guard performance metrics and goals to improve accuracy and timeliness, which should help to reduce improper payments.

(3) Civilian Pay. Reviews indicate improper payments have decreased in civilian pay over recent years; however, efforts to identify and reduce actions contributing to net pay errors continue. For FY 2007, civilian pay account reviews project an estimated \$7.1 million (.02%) in annual improper payments out of approximately \$29 billion in net pay to civilian employees. However, based on findings from the special review of military pay collections, a similar review was conducted for civilian pay accounts. This special review and subsequent data extract of civilian in-service collections revealed approximately \$68 million in additional improper payments. Therefore, the total improper payment estimate for civilian pay, including collections and adjusting sample results as needed to prevent over-estimation, is approximately \$75 million (.26%) of net pay. The improper payments that resulted in collection actions are primarily attributed to untimely and inaccurate reporting of time and attendance, personnel actions, and pay allowances. The Pay and Personnel Council serves as a forum to address civilian pay problem areas and seek methods to mitigate risks and reduce improper payments. Civilian pay metrics and corresponding accuracy and timeliness goals have been developed at the Component level and serve as a baseline for corrective action plans.

(4) Military Retirement. Payments to deceased retirees continue to be the highest risk for improper payments in military retired pay. Based on FY 2007 reviews, the Department projected approximately \$49 million in improper payments for this program, with almost the entire amount paid to deceased retirees. This represents an overpayment rate of .13% of the estimated \$37 billion in annual military retirement payments. In certain situations, payment to deceased retirees is unavoidable due to payment cycle dates and the fact that notifying a payroll activity is not likely to be the first action for next-of-kin at the time of a retiree's passing. A review of confirmed payments to deceased retirees in FY 2007 indicated that the Department recovered 93% of the overpayment amounts within 60 days, demonstrating the effectiveness of controls within the retired pay system once a retiree's death confirmation is received and processed for final disposition.

The Department's control processes to prevent, identify, and reduce overpayments to deceased retirees include a series of periodic eligibility notifications, early detection data mining efforts, and partnerships with other Federal and state entities. The Department routinely compares retired and annuity payroll master file databases to Social Security Administration "deceased" records and periodically compares records with the Office of Personnel Management deceased files. The file comparisons are also conducted with the Department of Veterans Affairs' cemetery database and with individual states with sizable retiree and annuitant populations (e.g., Texas, California, and Florida). Retirees identified as deceased in these comparisons must validate their continued eligibility, or the accounts are suspended.

(5) Travel Pay. The Department performs monthly random post-pay reviews of the Defense Travel System (DTS) and regularly reports the results to management. Reports address accuracy rate trends, over- and underpayment dollar amounts, reasons for errors, and recommendations for corrective actions to alleviate similar errors in the future. Results from reviews of trip records performed during FY 2007 revealed an estimated \$22 million (.91%) in improper payments out of a travel settlement population value of \$2.4 billion in DTS disbursements.

The Air Force's reviews of Reserve Travel System (RTS) vouchers for FY 2007 resulted in an estimate of \$19 million (1.6%) in improper payments out of \$1.2 billion in total payments for the year. Erroneous payments identified in RTS are sent to the appropriate Air Force bases for corrective actions (including collections or supplemental payments). The Air Force bases confirm corrections are completed. Also, a report of commonly identified errors is sent to all Air Force bases as a training tool. In the future, the Air Force plans to process all vouchers through DTS.

The other Active Duty Components (Army, Navy, and Marine Corps) primarily use the Integrated Automated Travel System (IATS) for travel payments not processed through DTS. Army payments are centrally processed through IATS with the exception of two offices that process a limited amount of travel payments. In FY 2007, Army IATS payments were reviewed against DTS payments to identify any duplicate payments between the two systems. The Department is implementing a sampling and review process for Army IATS in FY 2008 that meets the improper payment reporting requirements. Additionally, the Department is working with Navy and Marine Corps to ensure an adequate sampling and review process is developed and implemented in FY 2008 for their travel payments processed outside DTS. It is worth noting, however, that DTS implementation recently has been expanding exponentially throughout the Department. As DTS functionality expands, Components will continue transitioning away from the legacy systems.

Reviews of travel payment vouchers settled outside DTS for the U.S. Army Corps of Engineers (USACE) in FY 2007 resulted in approximately \$770 thousand (.5%) in improper payments out of approximately \$166 million in annual payments. The majority of these improper payments are due to traveler input errors and the failure of approving officials to properly review the voucher prior to payment. During FY 2007, all travel approving officials completed certification training. Additionally, the audit function will be consolidated at the USACE Finance Center in FY 2008. This should ensure greater consistency and accuracy in the audit of temporary duty travel vouchers.

#### IV. Program Improper Payment Reporting

The following table summarizes the Department's improper payment reduction outlook and total program outlays (payments) from FY 2006 through FY 2010.

Improper Payment Reduction Outlook

Program	FY 2006			FY 2007			FY 2008 Estimated			FY 2009 Estimated			FY 2010 Estimated		
	Outlays (\$ B)	IP (%)	IP (\$ M)	Outlays (\$ B)	IP (%)	IP (\$ M)	Outlays (\$ B)	IP (%)	IP (\$ M)	Outlays (\$ B)	IP (%)	IP (\$ M)	Outlays (\$ B)	IP (%)	IP (\$ M)
Military Health Benefits (Notes 1-4)	\$8.7	0.96	\$83.5	\$7.8	2.0	\$156.0	\$8.9	2.0	\$178.0	\$9.4	2.0	\$188.0	\$8.9	2.0	\$178.0
Military Pay (Notes 5)	\$72.4	0.09	\$65.9	\$72.9	0.51	\$370.0	\$75.7	0.46	\$349.6	\$68.4	0.46	\$314.6	\$69.7	0.45	\$313.4
Civilian Pay (Notes 6-7)	\$33.2	0.05	\$16.7	\$29.2	0.26	\$74.6	\$29.7	0.25	\$73.8	\$30.8	0.24	\$73.0	\$31.8	0.23	\$72.3
Military Retirement	\$35.9	0.14	\$49.4	\$37.1	0.13	\$48.7	\$39.6	0.13	\$51.2	\$41.3	0.13	\$51.9	\$42.9	0.12	\$52.3
Travel Pay (Notes 8-9)	\$5.2	0.80	\$29.4	\$5.8	1.00	\$43.6	\$6.8	1.00	\$68.0	\$6.8	1.00	\$68.0	\$6.8	1.00	\$68.0

IP – Improper Payments, B – Billions, M – Millions

Accompanying table notes can be found at <http://www.defenselink.mil/comptroller/afr/fy2007/FY07AFRSection3IPIA.pdf>.

## V. Recovery Auditing Reporting

The Department utilizes a number of different mechanisms to prevent, identify, and collect improper payments, to include recovery and contract auditing.

**Recovery Auditing.** The Department maintains an extensive post-payment process for identifying improper payments. This process utilizes post-payment review techniques performed both internally and by recovery auditing contractors paid from the proceeds actually recovered. Agency-wide commercial payments result in a large volume of transactions and high dollar values, so DoD maintains vigilance to ensure payment accuracy, using various manual and automated prepayment initiatives to prevent over- and underpayments.

Commercial pay overpayments identified for recovery are attributable primarily to internal recovery audit efforts and other means (including contract reconciliation and statistical sampling). Selected high dollar value payments are reviewed manually, and periodic independent reviews of commercial payments improve improper payment detection, correction, and prevention efforts.

The Department's Mechanization of Contract Administration Services (MOCAS) system, used for contract payments, processed 59% of the \$320 billion in DFAS commercial pay disbursements for FY 2007. Reviews of this system accounted for 69% (\$232.8 million) of the total \$338.4 million in improper commercial payments identified by DFAS for FY 2007. Over half of this total was underpayments. The Department disbursed approximately \$174 million in FY 2007 and \$210 million in FY 2006 to correct the identified underpayments. For FY 2006 and FY 2007, MOCAS system reviews identified \$66.2 million

in improper overpayments, of which \$59.2 million has been recouped. The Department also recouped \$18.6 million in commercial overpayments through contract recovery audits since 1996.

In addition to the amounts identified through recovery efforts, voluntary refunds received in FY 2006 and FY 2007 accounted for approximately \$125 million in collections. The DFAS continues to work with the Defense Agencies to improve the unsolicited refund process through improved identification and classification of the root causes of improper payments and take appropriate preventative actions.

The Department also has utilized a recovery audit contractor to identify for recapture overpayments made to hospitals that failed to submit amended cost reports from calendar years 1992 through 1997. These reviews have helped to recoup almost \$23 million in overpayments.

The Department has recovered \$30 million (99.9%) of the overpayments identified by the USACE during FYs 2004 through 2007. These recoveries are a result of reviews of payments, as well as vendor voluntary refunds. The two programs with the most identified overpayments pertain to military leases and utility payments. The USACE manages the Military Lease Program for all military services. When leased property is sold or leases are terminated without timely notifications, extra payments may be made. The USACE helps correct the error and notifies the Military Service. The USACE also manages the utility payments for the Department. When there is a merger or acquisition of utility companies, payments may be made before USACE is aware of changes to the payee information. To reduce the likelihood of these errors, USACE monitors the news for pending/new acquisitions and mergers of utility companies.

Recovery Audit Activity (amounts in millions)	Departmental Recovery Audit Totals (Note 1)	DFAS Agency-wide Commercial Payments (Note 2)	Military Health Benefits Recovery Audit Contractor
Amount Subject to Review for FY 2007 Reporting	\$189,300	\$189,300	\$0
Actual Amount Reviewed and Reported (FY 2007)	\$189,300	\$189,300	\$0
Overpayment Amounts Identified for Recovery (FY 2007)	\$24.6	\$24.6	\$0
Amounts Recovered (FY 2007)	\$19.6	\$18.9	\$0.7
Overpayment Amounts Identified for Recovery (Prior Years)	\$65.9	\$41.6	\$16.1
Amounts Recovered (Prior Years)	\$69.6	\$40.6	\$20.8
Cumulative Amounts Identified for Recovery (FY 2007 and Prior)	\$90.5	\$66.2	\$16.1
Cumulative Amounts Recovered (FY 2007 and Prior)	\$89.2	\$59.5	\$21.5

Note 1: The Department recovery audit totals include \$8.2 million in prior year recoveries (\$6.3 million in FY 2004 and \$1.9 million in FY 2005) from a recovery audit contract that concluded in FY 2005.

Note 2: The \$189.3 billion represents the total dollar value of disbursements (payments) in the MOCAS system, which includes 59% of the dollars disbursed by DFAS for commercial pay. There were \$59.1 million in overpayments and \$173.7 million in underpayments reported for MOCAS. Underpayments are not subject to recovery action. In accordance with IG recommendations, the identified recoveries do not include voluntary repayments of overpayments from vendors (these amounts were included in reporting in prior years). Cumulative amounts reflect totals from FYs 2006 and 2007, since detailed information on collections by type (to exclude voluntary repayments) is not readily available for FY 2005 and prior.

Additionally, many major companies now notify the USACE and the customer directly. Queries of related USACE databases help ensure records are modified promptly upon receipt of change notifications.

The Department of the Navy, Office of the Chief Information Officer, conducted a pilot recovery audit in FY 2006 on a sample of Navy telecommunications invoices. The results of the pilot indicated that a full recovery audit initiative might deliver a number of benefits to the Navy and assist in the ongoing implementation of its Telecommunications Management and Action Plan. A recovery audit contractor began work in early calendar year 2007 to examine all local, long distance, and data-related telecommunications costs. The program currently remains in its initial stages and no funds yet have been recovered or identified as recoverable.

**Contract Auditing.** The Defense Contract Audit Agency (DCAA) routinely performs billing system audits at major contractors (e.g., contractors with a substantial amount of flexibly priced contracts and fixed price contracts) to determine the adequacy of the contractor's billing system internal controls and its compliance with those controls. This effort provides assurance to the Department that the contract payment billings are based on costs incurred and approved provisional billing rates. The DCAA also performs paid voucher reviews at major contractors and special purpose audits at contractor locations when an improper payment risk factor is identified and neither a billing system review nor a test of paid vouchers is planned.

## **VI. Accountability**

Certifying officer legislation holds certifying and disbursing officers accountable for government funds. In accordance with Section 2773a of Title 10, United States Code, pecuniary liability attaches automatically when there is a fiscal irregularity, i.e., (1) a physical loss of cash, vouchers, negotiable instruments, or supporting documents, or

(2) an improper payment. Efforts to recover from a recipient must be undertaken in accordance with the debt collection procedures in Volume V, Chapters 29 and 30, of the DoD Financial Management Regulation.

## **VII. Infrastructure**

The Department has the information and infrastructure needed to reduce improper payments in each of the improper payment program areas. The Department also is implementing a Business Activity Monitoring service which will employ the latest technology to increase the efficiency and effectiveness of improper payment detection efforts for commercial pay.

## **VIII. Barriers**

The Department did not identify any program areas facing statutory or regulatory barriers limiting corrective actions.

## **IX. Additional Comments**

The OMB requested the Department identify Iraq improper payment indicators. In support of this request, DFAS and the USACE have conducted additional reviews on payments for Iraq.

At the recommendation of the IG, DFAS initiated a review of in-service collections in FY 2007. Findings confirmed that these collections were related to initial improper payments. Therefore, special reviews of these populations are ongoing for military pay and civilian pay collections. Results of these new reviews are included in improper payments reporting.

Details about these special reviews can be found at <http://www.defenselink.mil/comptroller/afr/fy2007/FY07AFRSection3IPIA.pdf>.