DEFENSE HEALTH PROGRAM

AGENCY FINANCIAL REPORT

FISCAL YEAR 2021

Introduction

Agency Head Message

After nearly 21 months of operating under a national emergency with the Coronavirus Disease 2019 (COVID-19) pandemic, the Military Health System (MHS) continues to focus on our top priority—providing the highest quality healthcare possible to ensure the medical readiness of our warfighters, and keeping their families healthy and safe. That is the purpose for which our MHS exists and the reason why it's vital that we invest time and effort into properly stewarding our Defense Health Program (DHP) resources.

This report comes at a time of unprecedented challenges as we tackle the COVID-19 pandemic. During the past year, COVID-19 has been our number one priority. Military medicine has been leading efforts to protect our workforce, maintain readiness, and support the national response. Whether it was standing up a COVID-19 Testing Task Force, collecting more than 10,000 units of COVID Convalescent Plasma, or distributing and administering the COVID-19 vaccine, the MHS continues the fight against COVID-19.

We have also continued to make tremendous progress on our high priority MHS initiatives.

Implementing TRICARE Reform. Our patients benefitted from recent TRICARE enhancements—including a successful rollout of two TRICARE Open Seasons; transition of more than 450 military hospitals and clinics to the TRICARE.mil website; and expansion of telehealth services specifically to meet patient needs during the pandemic.

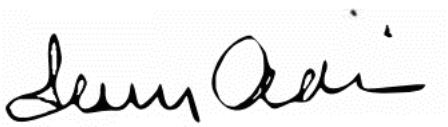
Continuing MHS GENESIS Rollout. The MHS continued its expansion of MHS GENESIS to our military treatment facilities (MTFs). MHS GENESIS integrates inpatient and outpatient solutions that connects medical and dental information across the continuum of care, from point of injury to the MTF. When fully deployed by fiscal year (FY) 2024, MHS GENESIS will provide a single health record for Service members and their families.

Implementing MTF Transition to the Defense Health Agency (DHA). Great strides were taken in FY 2021 to transition MTFs from the Military Departments to the authority, direction, and control of the DHA. This transition is designed to increase overall access to care for beneficiaries; improve coordination, standardization, and dissemination of best practices across the MHS; and provide more opportunities for military medical providers to get the training they need to meet readiness goals. The MHS is on track to complete this transition early in FY 2022.

The outcome of our fourth audit proves that we are committed to using the audit as a valuable learning tool. While we are pleased to have achieved another unmodified opinion in FY 2020 on DHP funds allocated to our private sector/TRICARE programs (11th consecutive year in a row reported through the financial statements of the Defense Health Agency – Contract Resource Management); we recognize that we still have a considerable amount of work to do on our direct care MTF programs. We are continually using the results of our financial statement audits to build a body of evidence that justifies the overhaul of ineffective policies and procedures, to invest in tools and enablers that improve oversight, and to assign subject matter experts to develop and implement well-designed controls to mitigate risks. These efforts are aimed at producing the eventual, desired internal control environment.

Focusing on producing verifiable evidence to support our financial reporting is vital. Our management infrastructure and decision-making rely heavily on data—whether it's financial, clinical, or managerial. Data is a strategic asset to the organization, therefore, not only must it be credible; it must also be accurate. Verifying that data is accurate demands that evidence be produced and tested. Whether testing is done by external auditors or through internal self-inspections, the objectives are the same—that we learn from the results so that we can improve.

As a medical organization, we wholeheartedly recognize that we must steward our resources and will continue to harness the array of talent within our workforce to evaluate how well policies and programs are working, and to explore innovative ways to achieve our medical mission in a financially transparent and accurate manner. Transparency and accountability support sound stewardship of taxpayer funds and compels financial management rigor, integrity and efficient and effective business practices. This too is our responsibility and obligation to our nation.



Terry Adirim, M.D., M.P.H., M.B. A.

Acting Assistant Secretary of Defense for Health Affairs

About the Agency Financial Report

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 is prepared pursuant to the following guidance which requires DHP to prepare an AFR:

- *Chief Financial Officers Act of 1990* (CFO Act, Public Law (P.L.) 101-576, codified as 31 U.S.C. §501 note) as amended by the *Government Management Reform Act of 1994* (GMRA, P.L. 103-356, codified as 31 U.S.C. §3301 note);
- Department of Defense (DoD) 7000.14R *Financial Management Regulation* (FMR)*, Volume 6B*;
- *Office of the Under Secretary of Defense (Comptroller) ((OUSD(C)) Memo, FY 2021 DoD Reporting Entities*;

This AFR uses the financial reporting requirements of the following:

- Office of Management and Budget (OMB) Circular A-136, *Financial Reporting Requirements*
- OMB Bulletin 21-04, *Audit Requirements for Federal Financial Statements*;
- Treasury Financial Manual (TFM) Volume I, Part 2, Chapter 4700, *Federal Entity Reporting Requirements for the Financial Report of the U.S. Government*; and
- OUSD(C) DoD Financial Reporting Guidance Attachment 103, *Standard Note Disclosures*.

The MHS chooses to produce an AFR rather than the alternative Performance and Accountability Report (PAR). The Annual Performance Report, with detailed performance information that meets the requirements of the *Government Performance and Results Modernization Act of 2010* (GPRAMA, P.L. 111-352), will be provided within the Annual Performance Plan and Report and transmitted with the release of the Congressional Budget Justification. The 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 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 DoD Office of the Inspector General (OIG).

Contents

Management's Discussion and Analysis

Section I

Mission and Organizational Structure

History

American military medicine traces its origins back to July 27, 1775. With more than 246 years of serving the nation's military medical needs, the MHS is one of America's largest and most complex healthcare institutions. The MHS supports the National Defense Strategy (NDS) by providing healthcare support for the full range of military operations. Our MHS saves lives on the battlefield, combats infectious disease around the world, responds to humanitarian efforts, and is responsible for providing health services to 9.6 million Department of Defense (DoD) healthcare beneficiaries. Services are delivered through both MTFs and contracts with private sector healthcare networks. MHS beneficiaries are comprised of uniformed Service members, military retirees, and family members.

Mission

"We, the Military Health System, enable the National Defense Strategy by providing a ready medical force, a medically ready force, and improve the health of all those entrusted to our care."

The MHS's 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, uniformed services retirees, certain members of the Reserve Components, family members, survivors, certain unmarried former spouses, and other eligible members. These MHS beneficiaries receive either direct care delivered by MTFs or private sector care purchased from civilian TRICARE network providers networks and non-network TRICARE authorized providers. In addition to MTF pharmacies, the TRICARE Pharmacy Program (TPharm) provides prescription and mail order coverage.

Our FY 2021 Unified Medical Budget (UMB)/DHP appropriation is aligned with the Department's vision of a more lethal, results-oriented DoD that possesses the capabilities and capacity to implement the National Defense Strategy (NDS). Every line of the DoD's FY 2021 budget is strategy driven and designed to support the Department's three primary lines of effort, which are to increase our military's lethality, strengthen our network of alliances and partnerships, and reform DoD's business practices for greater performance and affordability.

Central to increasing our military's lethality is to (1) ensure we have a properly trained and ready medical force so that we can (2) ensure our warfighters meet or exceed DoD's exacting healthcare requirements, while optimizing their health and driving improved human performance. The lethality of our warfighters begins with their physical and mental condition. Our medical workforce is entrusted with bolstering our warfighters' lethality by strengthening their survivability, resiliency, and readiness. Accordingly, the MHS workforce upholds the medical standards for deployability and

What is the Defense Health Program?

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 097 0130. All sums appropriated to carry out the functions of the Secretary of Defense with respect to medical and healthcare programs of the DoD 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 under *§ 1079, 1086, 1092 or 1097 of 10 U.S.C.*

The Assistant Secretary of Defense (Health Affairs) (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 and programs. The ASD(HA) serves as resource manager for all DoD health and medical financial and other resources and prepares the UMB for the annual President's Budget submission to request appropriations for the DoD 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 six MHS financial statement reporting components through the DHA. The six component reporting entities that make up 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, and (6) DHA.

affords our warfighters the medical resources necessary to confront and overcome the challenges of war.

Revamping business operations to strengthen our internal controls and achieve a clean audit opinion on our financial statements is an ongoing priority of the Department and demonstrates our ability to properly steward resources. We are actively reforming our business practices to close internal control gaps and comply with auditor recommendations.

Whether ensuring that warfighters are ready for deployment, treating a gunshot wound or depression, it is our privilege and our resolve to ensure our warfighters and all beneficiaries receive the medical care needed to maintain and restore their health.

Major Programs

Our major programs include more than just combat medicine – it also includes the following programs that together form a complex globally integrated system that enables us to accomplish our mission and deliver world class healthcare:

- **Healthcare delivery** both in garrison and during contingencies. This includes a focus on trauma care and developing interoperability with partner nations thru our global health engagements program. See *Figure 1* below for a summary of the number of healthcare delivery cases completed in FY 2020.
- **Public health and medical education** through the Medical Education and Training Campus and the Uniformed Services University of the Health Sciences (USUHS), we support the readiness of America's Warfighter and the health and well-being of the military community by educating and developing uniformed health professionals, scientists, and leaders; by conducting cutting-edge, military-relevant research, and by providing operational support to units around the world.
- **Private sector partnerships.** Building strong partnerships with our civilian healthcare sector through our TRICARE program is vital to our success.
- **Cutting-edge medical Research Development Test & Evaluation (RDT&E)** through the DHA's Research and Development directorate, the U.S. Army Medical Research and Development Command, the Air Force Research Laboratory, and through partnerships with various organizations, including those established with Cooperative Research and Development Agreements.

Figure 1: DHP MHS by the numbers – FY 2020.

Military Health System by the Numbers – FY 2020	
Type of Care	*Annual Workload Summary*
Inpatient Admissions	**Total: 870,700** ► Military Facilities: 166,800 ► TRICARE-authorized Facilities: 335,200 ► TRICARE For Life: 368,700
Outpatient Visits	**Total: 92,100,000** ► Military Facilities: 33,500,000 ► TRICARE-authorized Facilities: 31,700,000 ► TRICARE For Life: 26,900,000
Births	**Total: 105,500** ► Military Facilities: 32,900 ► TRICARE-authorized Facilities: 72,600
Prescriptions Filled	**Total: 108,100,000** ► Military Pharmacies: 37,600,000 ► Network Pharmacies: 23,800,000 ► Home Delivery: 5,000,000 ► TRICARE For Life: 41,700,000
Emergency Department Visits	**Total: 3,398,800** ► Military Facilities: 982,400 ► TRICARE-authorized Facilities: 1,426,100 ► TRICARE For Life: 990,300

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

Organization

Leading the MHS, is the Office of the Assistant Secretary of Defense for Health Affairs (OASD(HA)) as illustrated in *Figure 2* below. The ASD(HA) is a civilian, Senate-confirmed official who serves as the chief medical adviser to the Secretary of Defense and oversees health policy and budgeting across the system, as well as directing the activities of the Defense Health Agency. The ASD(HA) is supported by the Principal Deputy Assistant Secretary of Defense (PDASD) for Health Affairs and three Deputy Assistant Secretaries of Defense (DASD), consisting of (1) the DASD for Health Readiness Policy and Oversight (HRP&O); (2) the DASD for Health Resources Management and Policy (HRM&P); and (3) the DASD for Health Services Policy and Oversight (HSP&O). The ASD(HA) also maintains oversight of the Defense Health Agency (DHA) and the Uniformed Services University of the Health Sciences (USUHS).

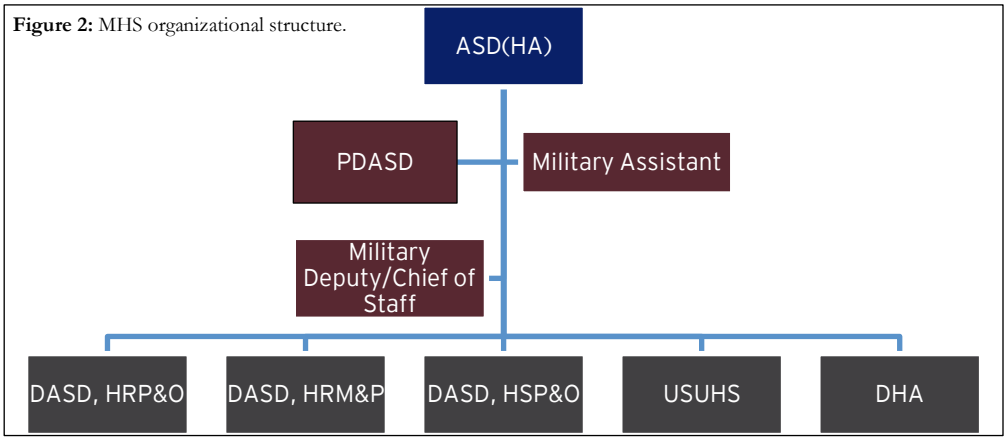


Figure 2: MHS organizational structure.

The ASD(HA) serves as resource manager for all DoD health and medical resources and submits the UMB as part of the President's budget submission to Congress. The UMB provides the financial resources the MHS requires to support the DoD's vision of a more lethal, results-oriented agency that possesses the capabilities and capacity to successfully implement the National Defense Strategy. The UMB consists of discrete parts that include:

- Preparation and submission of budget exhibits and justification materials for DHP appropriation.
- Input to the individual Military Department Military Personnel Appropriations (MPA) for all medical military personnel end-strength.
- Input to the DoD Military Construction (MILCON) appropriation for medical facility projects.

The ASD(HA) ensures DHP appropriation is allocated to the six components that comprise the MHS. The DHA, under the authority of the ASD(HA), distributes DHP funds to the components in the amounts approved within DHP Program Objective Memorandum (POM), and as mission requirements dictate. The components further sub-allocate the appropriation to their subordinate organizations. The six MHS components are:

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 maintains 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 four lines of effort to build readiness, modernize concepts and capabilities, reform processes, and strengthen our alliances and partnerships to ensure land power dominance on any battlefield, against any threat, at any time. 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 is a global healthcare network of highly trained medical personnel who provide healthcare support to the U.S. Navy, Marine Corps, their families, and veterans in high operational tempo environments, at expeditionary medical facilities, military treatment facilities (medical centers, hospitals, and clinics), hospital ships and research units around the world. BUMED is led by the Navy Surgeon General, and is headquartered in Falls Church, Virginia. The BUMED team of physicians, dentists, nurses, corpsmen, allied health providers, and support personnel also works in tandem with the Army and Air Force medical personnel and coalition forces to ensure the physical and mental well-being of service members and civilians. This care is provided via DHP and coordinated by the Office of ASD(HA) with support from the DHA.

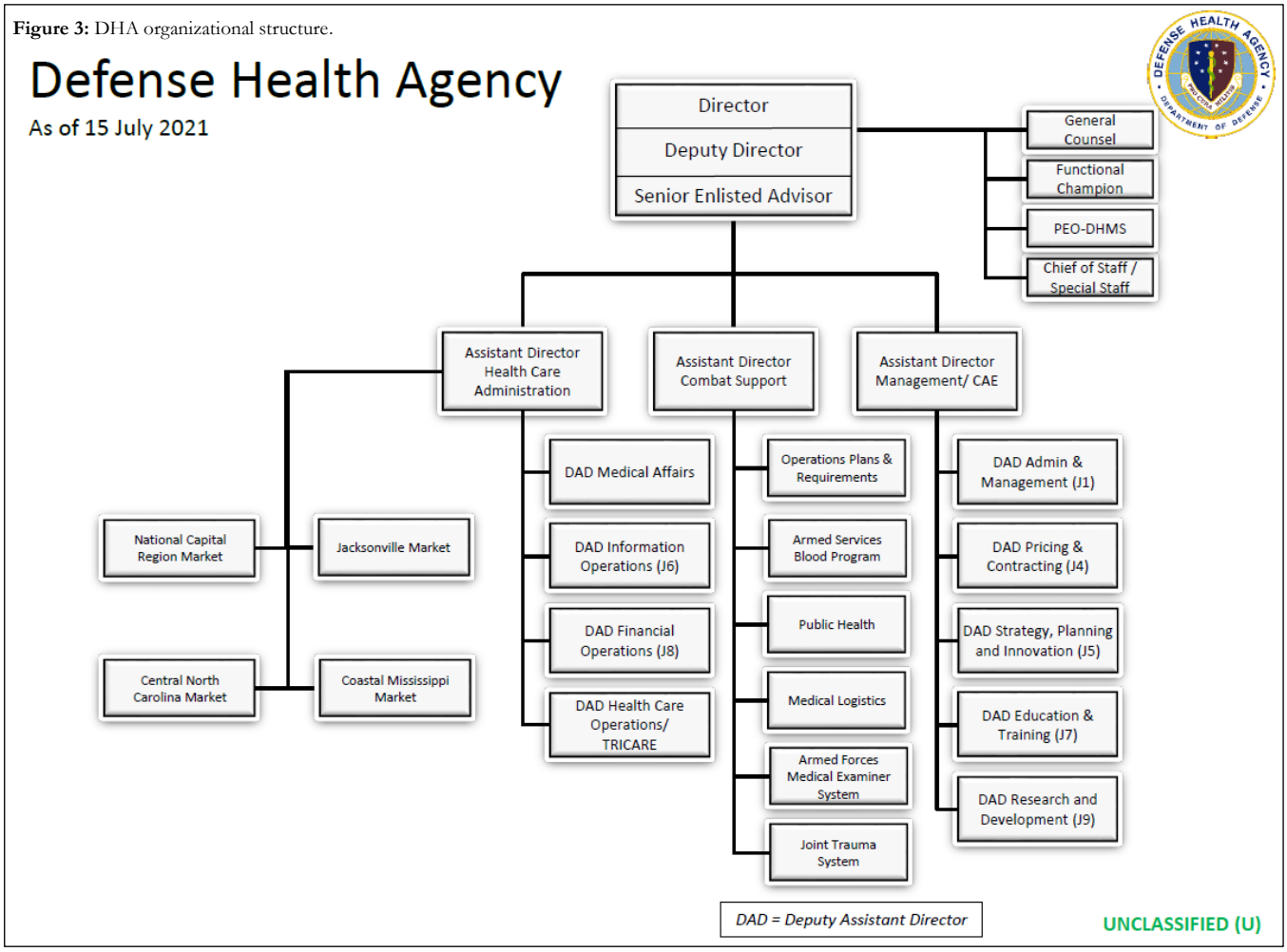
U.S. Air Force Medical Service (AFMS): The Air Force Medical Service supports the United States Air Force through the provisioning of full spectrum medical readiness delivering unique medical capabilities at home and abroad. Our priorities align with Air Force priorities to ensure mission success. We embrace our heritage of innovation and relentlessly pursue advances to enhance safety, effectiveness, and efficiency of care we deliver to beneficiaries and support we provide to Combatant Commanders. The AFMS Mission is to ensure medically fit forces, provide expeditionary medics, and deliver Trusted Care to all we serve. We are charged to ensure that all Air Force personnel are medically fit, physically, and psychologically resilient, and ready to meet AF mission requirements. We must organize, train, and equip expeditionary medics in support of the Joint Warfighter. We fulfill the Trusted Care principles of Leadership, Safety, Patient Centeredness, and Continuous Process Improvement for all we serve."

Defense Health Agency (DHA): DHA is a joint, integrated Combat Support Agency (CSA) that enables MEDCOM, BUMED, and the AFMS to provide a ready medical force and medically ready force to Combatant Commands (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 $45 billion DHP budgetary resources to support the delivery of integrated, affordable, high-quality health services to the DoD's 9.6 million eligible beneficiaries. The DHA drives greater integration of clinical and business processes across the contracted healthcare networks and MTFs. The DHA also 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. See *Figure 3* below for DHA's organizational structure.

Uniformed Services University of the Health Sciences (USUHS): The mission of USUHS is to support the readiness of America's Warfighter and the health and well-being of the military community by educating and developing uniformed health professionals, scientists, and leaders; by conducting cutting-edge, military-relevant research, and by providing operational support to units around the world. 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. USU is recognized as an essential source of highly qualified health care professionals with strong leadership skills and the capability to support medical readiness for our Nation and the Military Health Care System (MHS). USUHS is distinctive in its mission of graduating individuals who have learned to care for those in harm's way, whether that is through patient care, research, health policy, or health professions education. USUHS graduates are health professionals and leaders prepared with an outstanding health education, interprofessional health training, leadership training, and a deep and abiding commitment to selfless service, the uniformed services ethos, and the security of the United States.

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 electronically processes invoices received from its contractors and through the TRICARE Encounter Data System and reports 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 and prior years' spending and program developments. CRM uses DHP funds provided by annual appropriations to reimburse private sector healthcare providers for services rendered to TRICARE beneficiaries. In addition, CRM's Improper Payment Evaluations Branch conducts post payment audits. It also assists DHA's Contract Management, Program Integrity (PI) (fraud), and Case Recoupment division activities related to private sector care. **NOTE:** CRM is allocated nearly half of DHP appropriation, prepares its own financial statements, and is audited separately from DHP. **CRM is individually addressed as an entity in a separate AFR and therefore will be minimally addressed within the MD&A.**

Figure 3: DHA organizational structure.



MHS Governance

To effectively manage the MHS, the following governance structure has been established:

- Military Health System Executive Review Board (MHSER). The MHSER is the highest level MHS governing body for input into the strategic, transitional, and emerging issues facing the MHS, DHP, and the DoD with respect to the responsibilities and functions assigned to the USD(P&R) by *DoDD 5124.02*, *Under Secretary of Defense for Personnel and Readiness (USD(P&R))*. The MHSER promotes and facilitates the integration of MHS/DHP initiatives and plans with larger DoD/Service Line concerns and de-conflicts priorities of individual MHS Components. It enables direct information flow to senior Service Line military and civilian leadership and establishes a mechanism for input into matters being raised at the MHSER level.
- Senior Military Medical Advisory Council (SMMAC). The SMMAC serves as an advisory board to the ASD(HA) and is the highest level of the HA Governance structure. It presents enterprise-level guidance and operational issues for decision-making on final budget issues. The SMMAC adjudicates and approves issues and decisions.
- Deputy Military Medical Action Council (DMMAC). The DMMAC serves as the body for policy and program oversight and to adjudicate issues that span the MHS. This governance body is the key method through which HA performs oversight of the system, monitors the performance of the MHS, and provides decision support to the ASD(HA) through the SMMAC. The DMMAC is responsible for assessing system performance and providing recommendations to the ASD(HA) on aligning healthcare policies with performance. The DMMAC provides enterprise-wide strategic direction and oversight of:
  - Health and healthcare policies and programs;
  - MHS resource planning and allocation, including how requirements will be defined, programmed, and allocated to the Services and DHA;
  - Medical readiness policies and programs; and

  - Various health information systems, programs, and initiatives across the MHS, including policies and performance of key enterprise initiatives, such as modernization of the Electronic Health Record (EHR) (MHS GENESIS).
- Council of Colonels and Captains (CoC). The CoC supports the work of the DMMAC and serves as a liaison to the MHS Components. The CoC promotes joint communication and transparency and serves as the body to improve the quality and timeliness of evidence-based decisions in MHS governance. The CoC is a collaborative forum for representatives from all the MHS Components to identify, collect, and prepare issues requiring resolution or decision at the DMMAC. The CoC is responsible for properly vetting issues requiring resolution or decision at the DMMAC.

Support of the National Defense Strategy (NDS)

The MHS emphasizes a culture of performance where results and accountability matter, and in which MHS resources are allocated to clearly support the NDS. The NDS espouses four primary lines of effort:

- Increase lethality
- Strengthen alliances and partnerships
- Reform the Department
- Take care of our people

MHS Strategic Goals and Objectives

The Under Secretary of Defense for Personnel and Readiness (USD(P&R)) established strategic goals and objectives, as illustrated in *Figure 4*, mapped to the NDS lines of effort. Resourcing decisions must be made in the context of supporting these goals and objectives to compel achievement of the NDS.

Figure 4: MHS strategic goals and objectives.

MHS strategic goals	MHS strategic objectives
(1) Improve the readiness of the Force; (2) Improve uniformed medical provider readiness; (3) Improve health outcomes of the population we serve; and (4) Reform the MHS for better performance and value.	(1) Advance the currency and capability of uniform healthcare providers and teams (2) Improve individual and family health readiness (3) Strengthen partnerships with governments, academia, and leading health systems (4) Improve healthy behaviors, communities, and environments (5) Maintain and optimize markets, military treatment facilities, and support functions

The Defense Health Program Appropriation

When enacted, the annual Appropriations Act reflects the amount of funding appropriated for peacetime MHS operations via DHP appropriation. As established in *Title 10 U.S.C., § 1100*, DHP account (Treasury Account Symbol 097 0130) contains amounts appropriated to carry out the functions of the SecDef with respect to medical and healthcare programs of the DoD. The SecDef may obligate or expend funds from the account for purposes of conducting programs and activities under *10 U.S.C., Chapter 55*, including contracts entered into under *Sections 1079, 1086, 1092 and 1097*.

DHP appropriation is sub-divided as follows:

- **Operation and Maintenance (O&M) funds**: DHP O&M appropriation funding provides for worldwide medical and dental services to active forces and other eligible beneficiaries, veterinary services, occupational and industrial health care, specialized services for the training of medical personnel, and medical command headquarters.
- **Procurement funds**: DHP Procurement program funds acquisition of capital equipment in MTFs and other selected health care activities which include equipment for initial outfitting of newly constructed, expanded, or modernized healthcare facilities; equipment for modernization and replacement of uneconomically repairable items; and MHS information technology (IT) requirements.
- **Research, Development, Test and Evaluation (RDT&E) funds**: DHP RDT&E program is developed in response to the needs of the National Defense Strategy and Joint Capabilities Integration and Development System. The goal is to advance the

state of medical science in those areas of most pressing need and relevance to today's battlefield experience and emerging threats. The objectives are to discover and explore innovative approaches to protect, support, and advance the health and welfare of military personnel and individuals eligible for care in the MHS; to accelerate the transition of medical technologies into deployed products; and to accelerate the translation of advances in knowledge into new standards of care for injury prevention, treatment of casualties, rehabilitation, and training systems that can be applied in theater or in MTFs.

How We Accomplish Our Mission

In addition to receiving the resources via the UMB and DHP appropriation, the MHS provides care in government owned or leased MTFs focused on sustaining readiness of the medical force and the medical readiness of deployable forces. MTFs are the heart of military medicine, where military, civilian and contract personnel provide care for DoD healthcare beneficiaries and gain the skills and training to support operational units. With 49 inpatient hospitals and Medical Centers; more than 460 ambulatory care and occupational health clinics; 192 dental clinics, located on military installations around the world, the MHS is one of the nation's largest health systems – it operates more hospitals than any nonprofit hospital system in the nation, and would rank among the top five for-profit systems.

Additionally, the MHS purchases more than 65 percent of the total care provided for beneficiaries through tailored contracts, such as Managed Care Support Contracts responsible for the administration of the TRICARE benefit. The MHS also receives a transfer of funds from the Medicare-Eligible Retiree Health Care Fund (MERHCF). The MERHCF is an accrual fund to pay for DoD's share of applicable Direct Care and Private Sector Care operation and maintenance healthcare costs for Medicare-eligible retirees, retiree family members and survivors.

Organizational Reform

Directed in the *National Defense Authorization Act* (NDAA) for FYs 2017 and 2019, the MHS is undergoing its most significant transformation in decades. The reforms set forth in the NDAA change the structure of the healthcare benefit and the management of the MHS. Centralization for the management and administration of the MTFs under the DHA transform the MHS into an integrated readiness and health system, eliminates redundancies, and creates a common high-quality experience for our beneficiaries.

In accordance with the FY 2021 Secretary of Defense Memo, *Department of Defense Reform Focus in 2020*, the MHS transferred the Service Medical Readiness activities which occur outside of the MTFs to the Military Departments. These activities were previously funded by DHP appropriation. This transfer allows the medical force structure to meet the operational requirements in support of the NDS and support the Congressionally mandated reforms to the MHS. The transferred Medical Readiness programs have been identified as functions that would be more effectively and efficiently run by the Military Departments and support development of a Ready Medical Force without adverse impact to the delivery of healthcare in MTFs.

In early 2017, the DHA began preparing to assume responsibility for the administration and management of MTFs and Dental Treatment Facilities (DTFs) worldwide. The assumption of these responsibilities commenced on October 1, 2018 with the transition of 31 facilities scattered throughout the southeastern portion of the United States (U.S.). All other MTFs/DTFs in the U.S. transitioned in October 2019 to DHA oversight and management with support from the Military Departments as the DHA continues to build its management system's capacity. The Military Department support will be transitioned on a conditions-based approach to ensure that healthcare delivery and readiness is not impacted. The second phase, executed in FY 2021, will transition additional MTFs located overseas to the management control of the DHA with a target of DHA having full control of all MTFs/DTFs by October 2022.

MHS Transformation

In keeping with the NDAA mandates, the DHA is establishing a market-based structure to manage the MHS' hospital and clinics. A "Market" is a group of MTFs in a geographic area that operate as a system, sharing patients, providers, functions, and budgets across facilities to improve the coordination and delivery of healthcare services. These market organizations will be responsible for the medical readiness of the Service members and the healthcare of beneficiaries in their respective regions.

- **Large Markets** – Nearly two-thirds of the MHS' current patient encounters occur in 21 regions where large medical centers exist. These large markets will have centers of excellence for specialty care that can meet the needs of beneficiaries across regions.
- **Small Markets** – Another 16 markets are centered on inpatient community hospitals focused on providing ambulatory and some specialty and inpatient care across their regions.
- **Stand-Alone Organizations** – Stand-alone hospitals and clinics located outside a market region will be supported by a stand-alone organization.

Market Benefits

Readiness – The Market construct provides opportunities to optimize patients while increasing maintenance of readiness related skillsets for providers and healthcare teams.

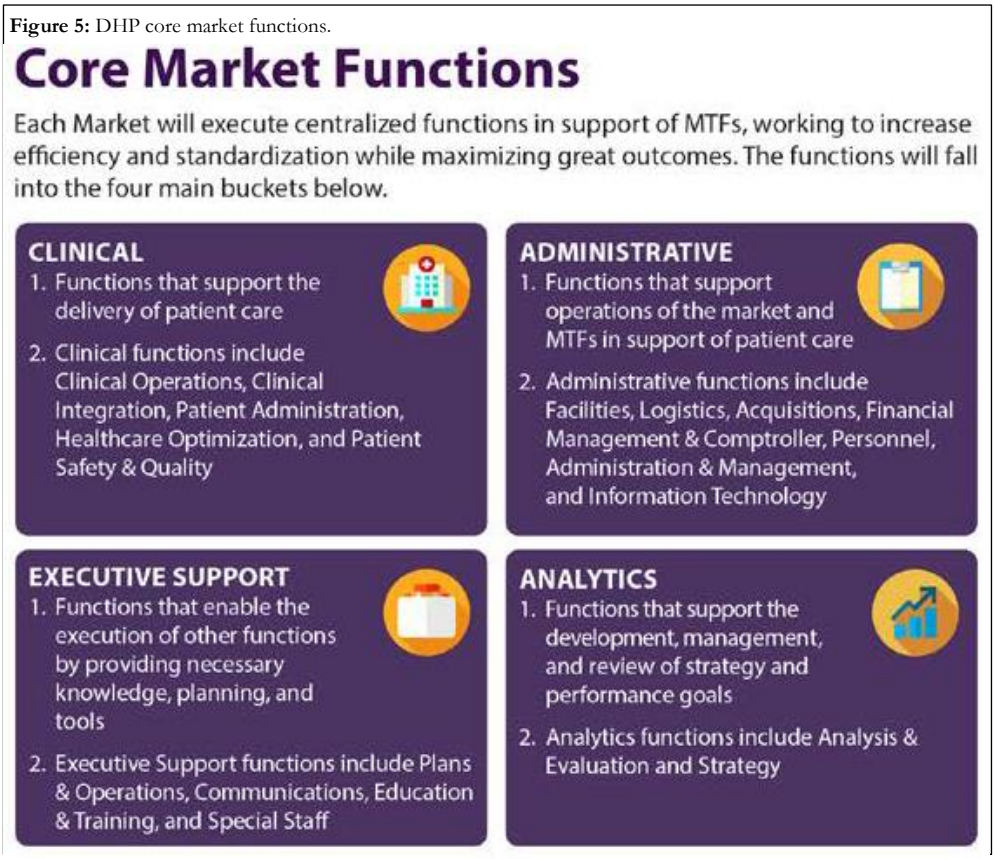
Patient Experience – The demand for specialties across the Market offers opportunity for aligning healthcare demand and supply. Standardized market initiatives provide greater consistency and convenience.

Staff Experience – Administrative functions are centralized across the Market, enabling staff to engage in enhanced skill development.

Resources – Resourcing (such as funding, personnel, and space) is optimized within the Market, creating flexibility for MTFs to launch broader initiatives within greater reach.

See *Figure 5* below for the centralized functions the Markets executer in support of the MTFs.

Figure 5: DHP core market functions.



Beneficiary Trends and Demographics

The Office of the ASD(HA) (OASD(HA)) together with the DHA, USUHS, MEDCOM, AFMS, and BUMED enables the provision of healthcare services to all of DoD and eligible beneficiaries. In FY 2020, 9.6 million beneficiaries were eligible for DoD medical care, including Active-Duty and their families, survivors, and certain former spouses. *Figures 6-9* below are excerpts from the FY 2021 *Evaluation of the TRICARE Program* Report[1] and provide a summary of the trends and demographics of eligible beneficiaries of DHP's services. Due to the release date of the *Evaluation of the TRICARE Program* Report, not all figures present FY 2021 amounts. However, the latest information available has been presented.

[1] *https://health.mil/Military-Health-Topics/Access-Cost-Quality-and-Safety/Health-Care-Program-Evaluation/Annual-Evaluation-of-the-TRICARE-Program*

Figure 6: MHS beneficiary trends and demographics.

BENEFICIARY TRENDS AND DEMOGRAPHICS

System Characteristics

TRICARE FACTS AND FIGURES—PROJECTED FOR FY 2021

	PROJECTED FOR FY 2021[a]	FY 2020 (AS PROJECTED LAST YEAR)
Total Beneficiaries	**9.6 million worldwide[b]**	9.6 million worldwide[b]
MILITARY FACILITIES—DIRECT CARE SYSTEM[c]		
Inpatient Hospitals and Medical Centers[d]	**49 (32 in U.S.)**	50 (37 in U.S.)
Ambulatory Care and Occupational Health Clinics	**465 (373 in U.S.)**	425 (372 in U.S.)
Dental Clinics	**192 (149 in U.S.)**	246 (203 in U.S.)
Veterinary Facilities[e]	**250 (185 in U.S.)**	251 (206 in U.S.)
Military Health System (MHS) Defense Health Program–Funded Personnel	**134,237**	138,283
Military	**77,317**	77,739
	27,495 Officers	28,824 Officers
	42,822 Enlisted	48,915 Enlisted
Civilian (including Foreign National)	**56,920**	60,544
CIVILIAN RESOURCES—PURCHASED CARE SYSTEM[f]		
Network Primary Care, Behavioral Health, and Specialty Care Providers (i.e., individual, not institutional, providers)[g]	**713,395**	548,297
Network Behavioral Health Providers (shown separately, but included in above)	**127,486**	97,727
TRICARE Network Acute Care Hospitals	**4,953**	4,372
Behavioral Health Facilities	**1,902**	1,612
Contracted (Network) Retail Pharmacies	**56,924**	56,696
Contracted Worldwide Pharmacy Home Delivery Vendor	**1**	1
TRICARE Dental Program (TDP) (for Active Duty families, Reserve members and their families)	**Over 1.84 million covered lives in 761,000 contracts**	Over 1.8 million covered lives in 769,000 contracts
TDP Network Dentists	**Over 72,000 total dentists, including: 57.5K general dentists over 14.5K specialty dentists**	Over 73,000 total dentists, including: 60,000 general dentists over 14,000 specialty dentists
Total Projected FY 2021 Unified Medical Program (UMP) (including Projected Trust Fund Receipts)	**$50.53 billion[h]**	$49.20 billion[h]
Projected Receipts from Medicare-Eligible Retiree Health Care Fund (MERHCF) Trust Fund	**$8.37 billion**	$7.53 billion

[a] Unless specified otherwise, this report presents budgetary, utilization, and cost data for the Defense Health Program (DHP)/UMP only, not those related to deployment or funded by the "Line" of the Services.

[b] Department of Defense (DoD) health care beneficiary population projected for mid–fiscal year (FY) 2021 is 9,648,000, rounded to 9.6 million, and is based on the DoD Comptroller's Budget End Strength, the DoD Actuary's forecast of retiree populations and the historical counts of family members per sponsor from the Defense Manpower Data Center (DMDC) End FY 2020 Defense Enrollment Eligibility Reporting System (DEERS) file.

[c] Military medical treatment facility (MTF) clinic count includes occupational health, community-based, embedded behavioral health, Active Duty troop, centers of excellence, and joint DoD-Department of Veterans Affairs (VA) clinics, and excludes leased/contracted facilities and Aid Stations; MTF counts are consistent with Defense Health Agency (DHA)/Resources & Management (J-1/J-8)/Budget and Execution and Programming Divisions. Source: DHA/Strategy, Plans, and Functional Integration (SP&FI) (J-5)/Analytics and Evaluation Division, 11/23/2020.

[d] AHC-Vicenza, AF-C-366th MED SQ–Mountain Home, AF-ASU-31st MEDGRP-AVIANO, and Kimbrough Ambulatory Care Center–Meade originated as medical clinics. Due to COVID-19 initiatives, their status was expanded to inpatient facilites. They will return to medical clinics in FY 2021.

[e] All 250 Veterinary Facilities moved to Army Line as the DoD Executive Agent for Veterinary Services.

[f] As reported by the managed care support contractors (MCSCs) for contracted network provider and hospital data (12/4/2020), and by TRICARE Dental Office, Health Plan Execution and Operations for dental provider data (12/30/2019).

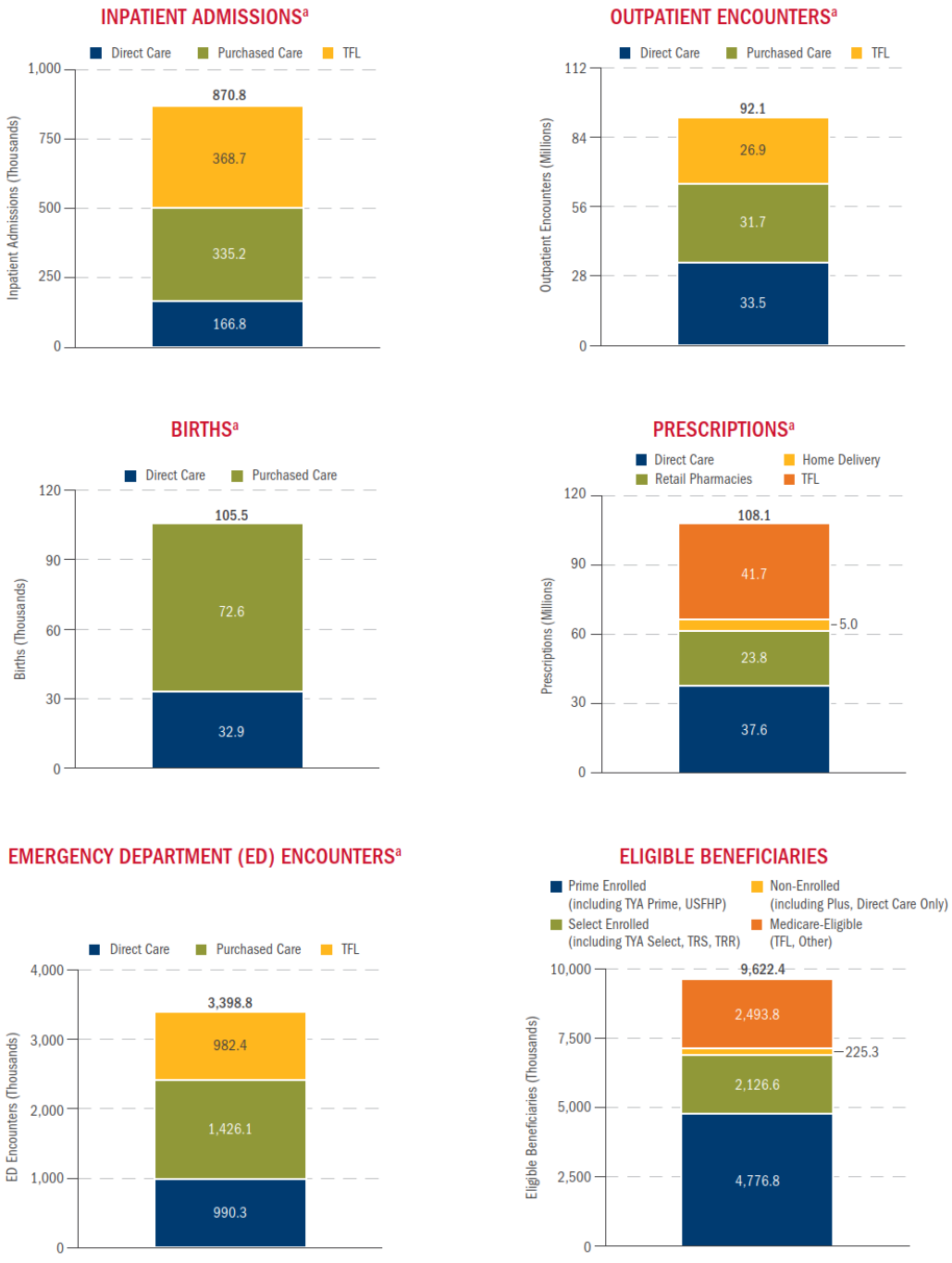
[g] This does not include 309,189 ancillary provider count.

[h] UMP presented here includes direct and private-sector care funding, military personnel, military construction, and the MERHCF ("Accrual Fund"). Budget and expense data from DHA/Resources & Management Directorate (J-8)/Budget & Execution Division, 9/30/2020.

Figure 7: MHS beneficiary trends and demographics (cont.).

BENEFICIARY TRENDS AND DEMOGRAPHICS *(CONT.)*

FY 2020 TRICARE Workload and Population Summary



Sources: MHS administrative data, 2/5/2021, and DEERS, 1/12/2021

[a] Excludes Uniformed Services Family Health Plan (USFHP) because MHS administrative data used in this report have no USFHP utilization information.

Notes:

– TFL=TRICARE for Life; TRR=TRICARE Retired Reserve; TRS=TRICARE Reserve Select; TYA=TRICARE Young Adult.

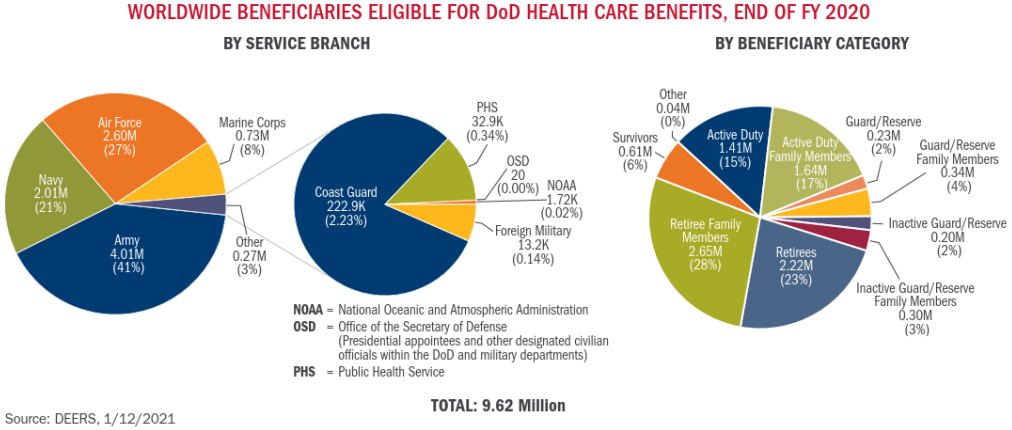
– Numbers may not sum to bar totals due to rounding.

Figure 8: Summary of eligible beneficiaries in FY 2020.

Eligible Beneficiaries in FY 2020

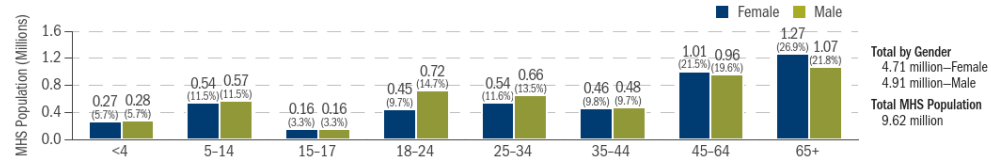
- There were a total of 9.62 million beneficiaries eligible for some form of DoD health care benefits at the end of FY 2020. The Army has the most beneficiaries eligible for Uniformed Services health care benefits, followed (in order) by the Air Force, Navy, Marine Corps, and other Uniformed Services (Coast Guard, Public Health Service, and the National Oceanic and Atmospheric Administration). Although the proportions are different, the Service rankings (in terms of eligible beneficiaries) are the same abroad as they are in the U.S.
- Retirees and their family members (including survivors) constitute the largest percentage of the eligible beneficiary population (57 percent). The U.S. MHS population is presented at the state level on page 42, reflecting those enrolled in the Prime benefit and the total population, enrolled and non-enrolled.
- Mirroring trends in the civilian population, the MHS is confronted with an aging beneficiary population.

WORLDWIDE BENEFICIARIES ELIGIBLE FOR DoD HEALTH CARE BENEFITS, END OF FY 2020



Source: DEERS, 1/12/2021
Note: Percentages may not sum to 100 percent due to rounding.

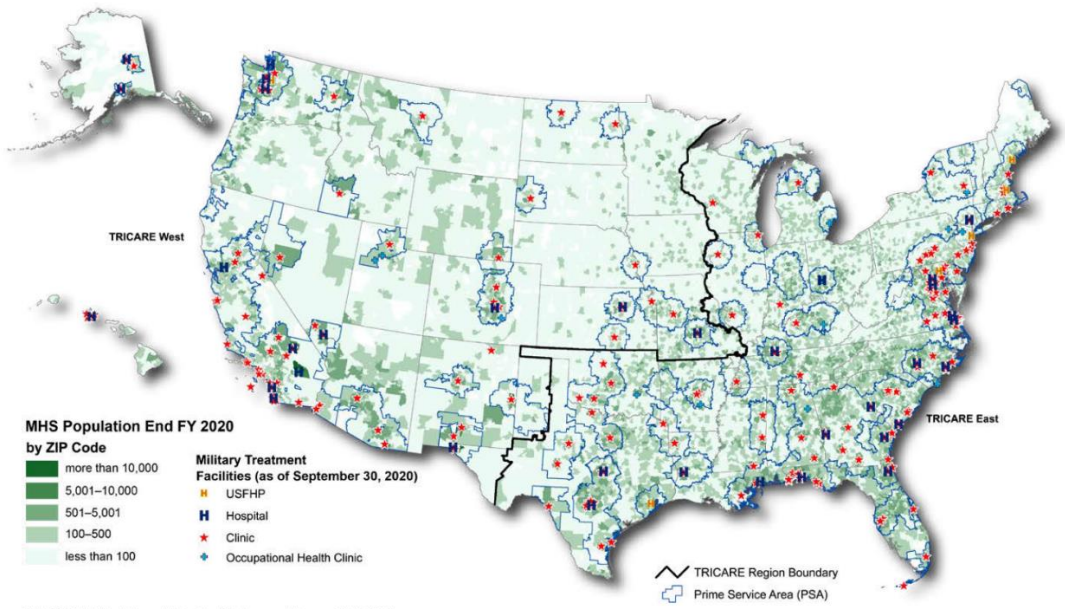
MHS POPULATION BY AGE GROUP AND GENDER, END OF FY 2020



Source: FY 2020 actuals from DEERS as of 1/12/2021

Figure 9: Beneficiary trends and demographics map.

MHS POPULATION DISTRIBUTION IN THE U.S. RELATIVE TO MTFs, END OF FY 2020



Source: DHA/SP&FI (J-5)/Analytics and Evaluation Division, population as of 1/19/2021
Note: For in-depth market area maps, visit https://info.health.mil/staff/analytics/decsupmp/gismaps (a DoD-issued Common Access Card [CAC] is required for access).

Analysis of Performance Goals, Objectives, and Results

Overview

DHP funds the MHS under the policy direction and guidance of the Assistant Secretary of Defense for Health Affairs (ASD(HA)). In 2009, the MHS adopted the Quadruple Aim of improved readiness, better health, better care, and lower cost for all components funded by the program. These aims are enduring. In 2019, the ASD(HA) released an enterprise strategy with three (3) goals for the MHS to focus improvement and drive modernization in accordance with the 2018 *National Defense Strategy*:

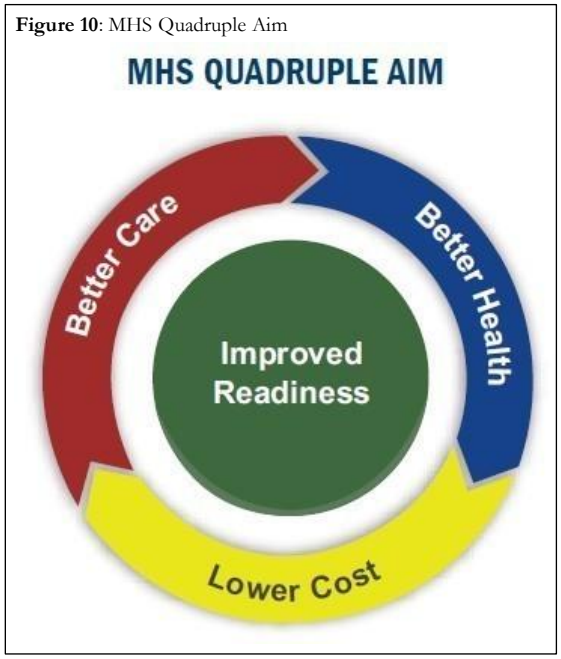
- **Goal 1:** Measure and improve the readiness of the force
- **Goal 2:** Measure and improve health outcomes of the population we serve
- **Goal 3:** Reform the MHS for greater performance and affordability

The strategy maintains alignment to the Quadruple Aim while providing more specific direction for the MHS components to ensure alignment to broader DoD goals. The DHA, SMAs, and USUHS have developed strategies and campaign plans to support the three goals of the MHS aligned to the Quadruple Aim. The ASD(HA) began revising the strategic performance management framework to improve oversight and assess the impact of major events facing the MHS. On top of routine health service delivery, in FY 2021 the MHS continued transitioning authority, direction, and control of MTFs from the Military Departments to the DHA; continued deploying a new electronic health record; provided patient care and public health measures in response to the COVID-19 pandemic; and supported Operation Allies Refuge.

The Quadruple Aim is illustrated in *Figure 10* and defined as:

- **Improved 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** is achieved 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.

Figure 10: MHS Quadruple Aim



Performance Information Assurance

The ASD(HA) selected 25 topline strategic measures to assess performance. The 25 strategic oversight measures were approved for reporting by the ASD(HA) on the advice and recommendation from the Senior Military Medical Advisory Council in 2020. Strategic performance measures often have a data lag of three to six months, given the inherent timelines for processing private sector healthcare claims, verifying record completeness, and analysis of millions of data points. *Figure 11* below summarizes the status and strategic alignment of each measure. Only available measures are reported and visualized as trendlines where relevant. Plans are in place to complete development of the remaining limited, prototyped, or in-development measures.

Figure 11: Status of strategic oversight measures.

Aim	MHS Goal	Measure Name	Status
Improved Readiness	Improve the readiness of the Force	Total Force without Deployment Limiting Medical Conditions	Available
		Active-Duty Days to Primary Care	Available
		Active-Duty Days to Specialty Care	Available
		Entire Population Primary Care	Available
		Entire Population Specialty Care	Available
		General Surgeons above Clinical Readiness Knowledge, Skills and Abilities Threshold	Available
		General Surgery Knowledge, Skills and Abilities generated by whole MHS	Available
Better Health	Improve Health Outcomes of the Population we Serve	Self-Reported Overall Health	Available
		Self-Reported Mental Health	Available
		Active-Duty Obesity Rate	Data Limited
		Tobacco Use Rate	Available
		Risk Adjusted Mortality	Available
Better Care		Near Miss to Harm Ratio	Available
		Total Harm Events	Available
		Inpatient Safety Composite (PSI90)	Available
		Recommend Hospital (Inpatient Satisfaction)	Available
Lower Cost	Reform the Military Health System for Greater Performance and Value	Cost per MTF Outpatient Encounter (RVU)	Prototyped
		Cost per MTF Inpatient Admission (MS-RWP)	Prototyped
		Cost per Beneficiary for HMO (TRICARE Prime)	Available
		Cost per Beneficiary for PPO (TRICARE Select)	Prototyped
		Cost per Beneficiary for Medicare (MERHCF)	Prototyped
		Total Private Sector Care Cost	Available
		Total Enrollees to MTFs	Available
		Net Deferrals from MTFs to Private Sector	Prototyped
		FTEs Available to the MTFs	In-development

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 repositories receive data from the legacy electronic health records (EHR) Composite Health Care System (CHCS) and Armed Forces Health Longitudinal Technology Application (AHLTA). The MHS is in the process of mapping data from the EHR MHS GENESIS to the repository. Given the complexity of the EHR implementation and data architecture, performance for some of these measures is not yet available at locations that have transitioned to MHS GENESIS.

Strategic data, trends, and information are populated on an interactive, web-based platform called CarePoint, accessible at: *https://carepoint.health.mil*. Unclassified data is available to MHS staff with a DoD Common Access Card (CAC) and HIPAA training. The CarePoint suite of tools pulls in data from the Medical Data Repository and is used primarily for managing local performance at markets and MTFs. *Figures 12-19* in the Strategic Performance section below were created using the information from the CarePoint suite. Due to delays in reporting underlying data, not all figures present yearend FY 2021 amounts. However, the latest information available has been presented. To improve independent oversight, the ASD(HA) is reporting strategic measures on the DoD Advana platform for senior leaders across the DoD. Advana is hosted by the Under Secretary of Defense (Comptroller).

The ASD(HA) conducts strategic deep dives as needed to analyze performance trends across the enterprise. Deep dives and their findings are shared with the Army, Navy, Air Force, DHA, Joint Staff, and USUHS through formal governance processes. A full evaluation of TRICARE is delivered to Congress annually with independent analysis conducted by a Federally Funded Research and Development Center (FFRDC).

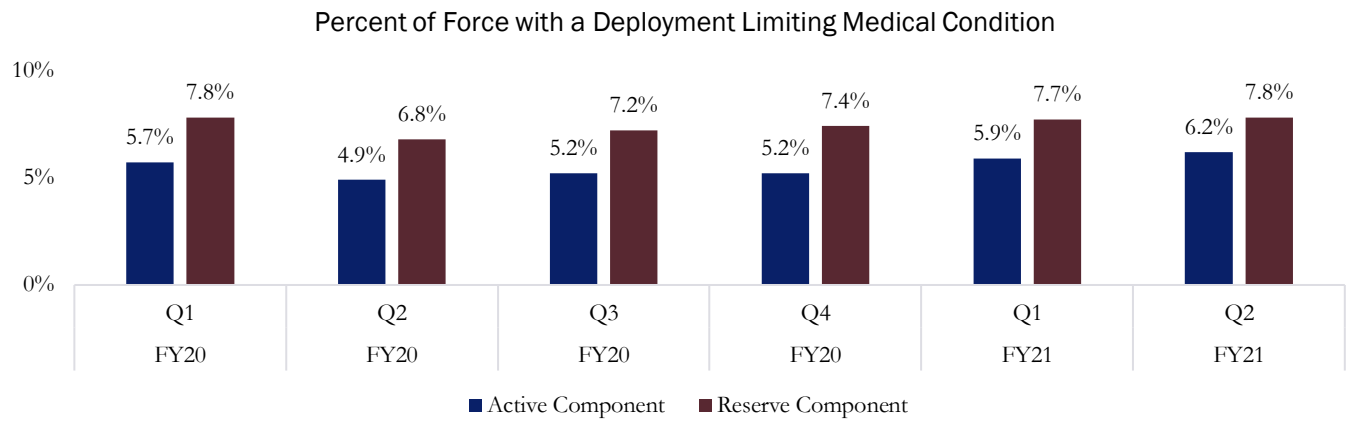
The information is organized by strategic goal. Dramatic changes in strategic performance from FY 2020 through 2021 may be attributable to the impacts of COVID-19 on American health service delivery organizations as well as associated force health protection guidance directed by the Office of the Secretary of Defense or data quality issues associated with MHS GENESIS.

Strategic Performance

Goal 1: Measure and improve the readiness of the force

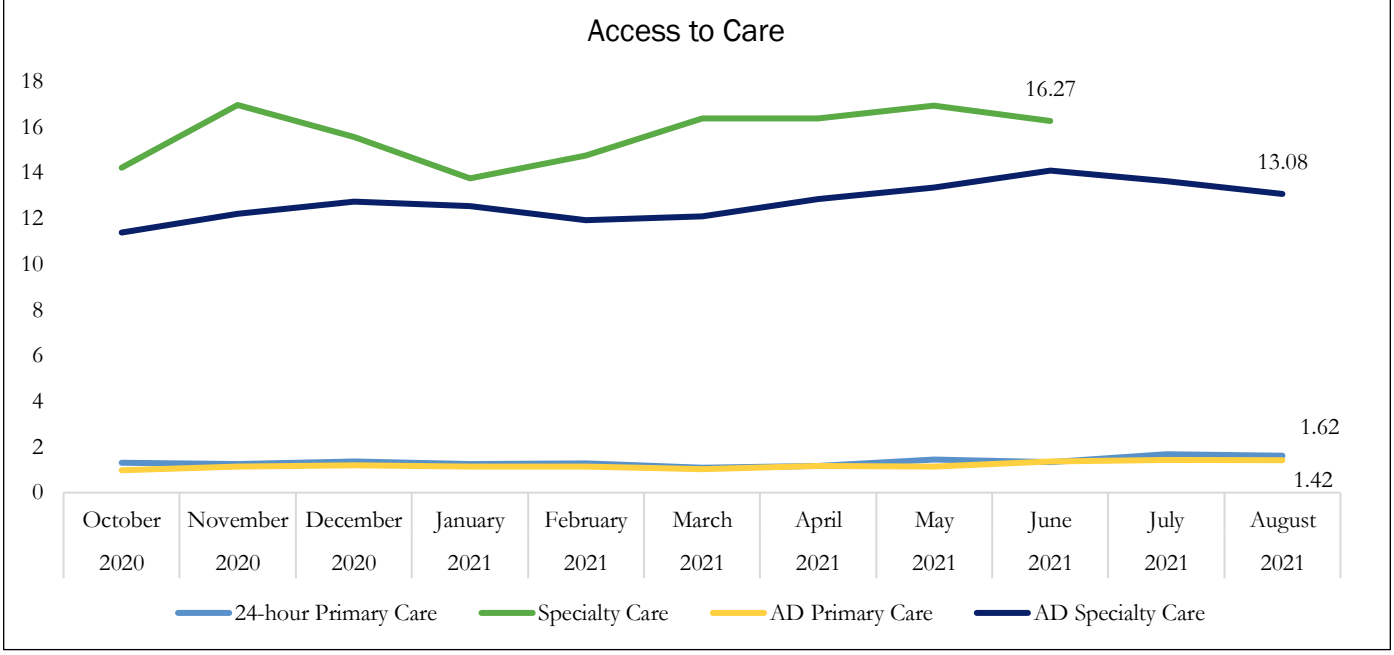
There are seven strategic performance measures for goal one. These metrics measure the medical readiness of the Total Force; indicate clinical capabilities of the medical force; and provide insight into accessibility of the MTFs for the Active Duty and other Prime-to-the-MTF beneficiaries. These measures are (1) total force with a deployment limiting condition; (2) Active-Duty access to primary care; (3) Active-Duty access to specialty care; (4) Prime population access to primary care; (5) Prime population access to specialty care; (6) general surgeons with clinical readiness knowledge, skills, and abilities (KSAs); and (7) general surgery KSAs generated by the MHS.

Figure 12: Percent of force with a deployment limiting medical condition.



The medical readiness of the Force is measured by the percent of the Total Force with a deployment limiting medical condition as illustrated in *Figure 12* above. Data are reported quarterly and organized by Military Department from FY 2020 through FY 2021, Quarter 2. DoD Instruction (DoDI) 6025.19, *Individual Medical Readiness* (IMR) with changes through May 12, 2020, governs individual medical readiness and reporting standards, including which diagnoses constitute a deployment limiting medical condition.

Figure 13: Access to care for force with a deployment limiting medical condition.



Access to care, a key component to ensuring a medically ready force, is measured by the number of days to a primary care and specialty care appointment for Active-Duty personnel and the number of days to the 3rd next available 24-hour care appointment and days between specialty care booking to appointment for the Prime and Plus populations receiving care from MTFs as illustrated in *Figure 13* above. DoDI 6000.14, *Patient Bill of Rights and Responsibilities* with changes incorporated through April 3, 2020 sets TRICARE Prime access standards. In accordance with policy, targets are less than 1 day for a 24-hour appointment and less than 28 days for a specialty care appointment.

Readiness of the medical force is proximally measured by the percent of general surgeons achieving their KSA threshold and the total number of KSAs generated by the MHS. Methodology was developed within the DoD by faculty at the USUHS. Using a rolling 12-month average as of August 2021, the MHS generated general surgery 36,206,816 KSAs. Due to changes in routine healthcare patterns from the COVID-19 pandemic, only 6% of general surgeons were at or above the KSA threshold. Data lags approximately six months. The KSA measures are unique to the military and not yet correlated to patient-level outcomes. As such, there is not yet a formal performance threshold and goal.

Goal 2: Measure and improve health outcomes for the population we serve

There are nine strategic performance measures for goal two. These metrics measure population health; healthcare effectiveness at MTFs; safety and high reliability at MTFs; and efficiency and effectiveness during transformation. The matured measures are: (1) self-reported overall health; (2) self-reported mental health; (3) adult obesity rate (data not available due to reporting issues); (4) adult tobacco use rate; (5) risk adjusted mortality; (6) near miss to harm events ratio; (7) total harm events; (8) inpatient safety composite; and (9) recommend hospital.

Figure 14: Self-reported overall and mental health.

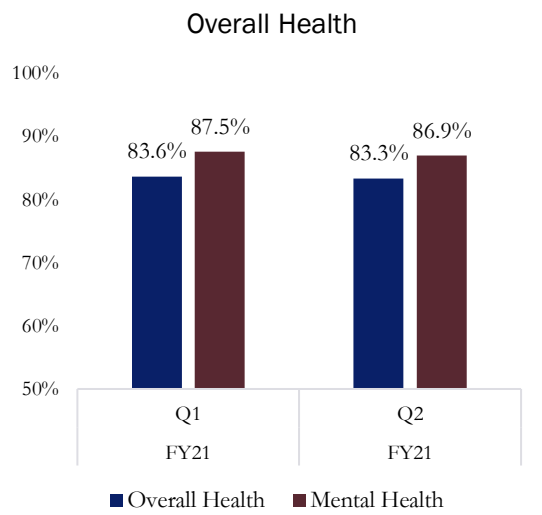


Figure 15: Adult tobacco use rate.

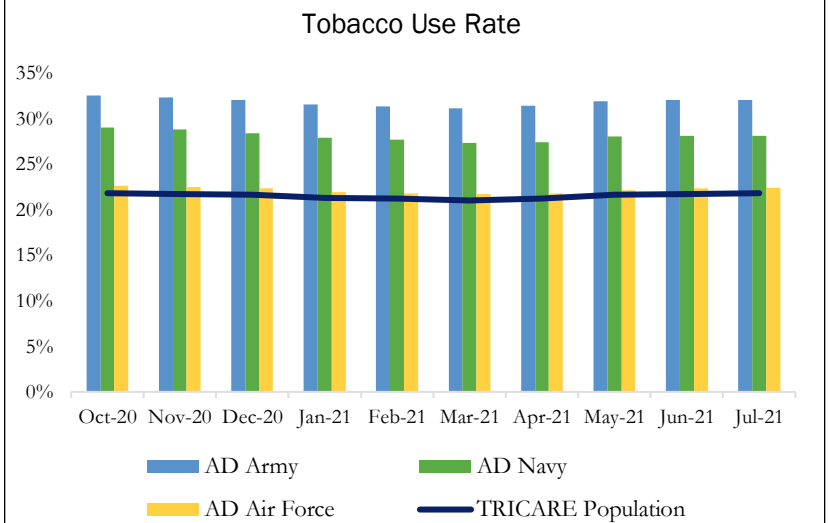
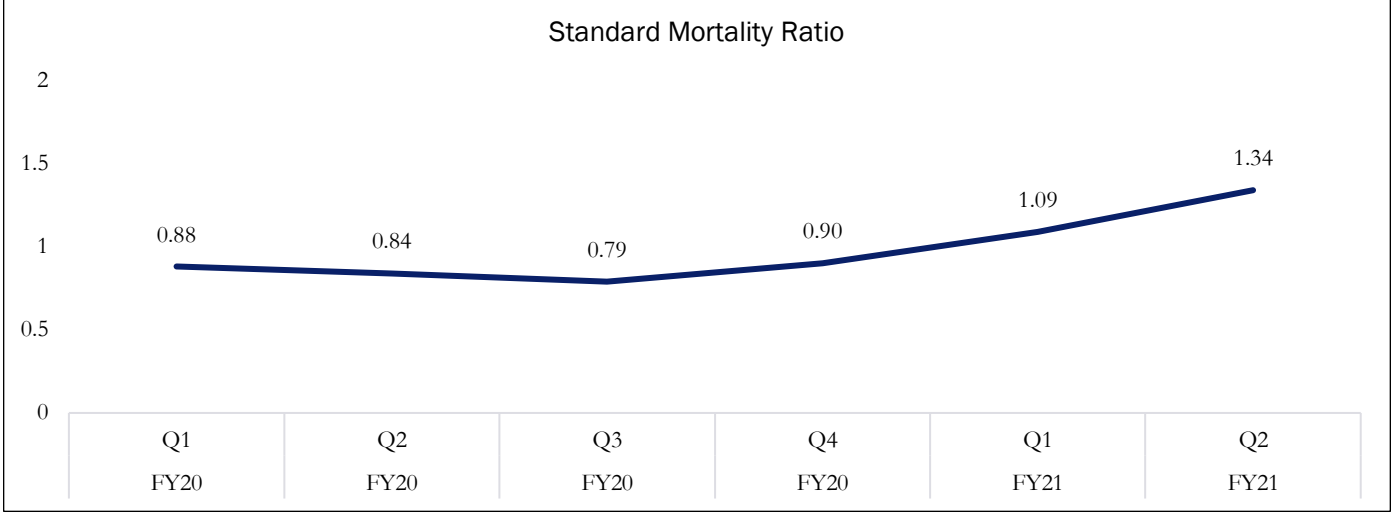


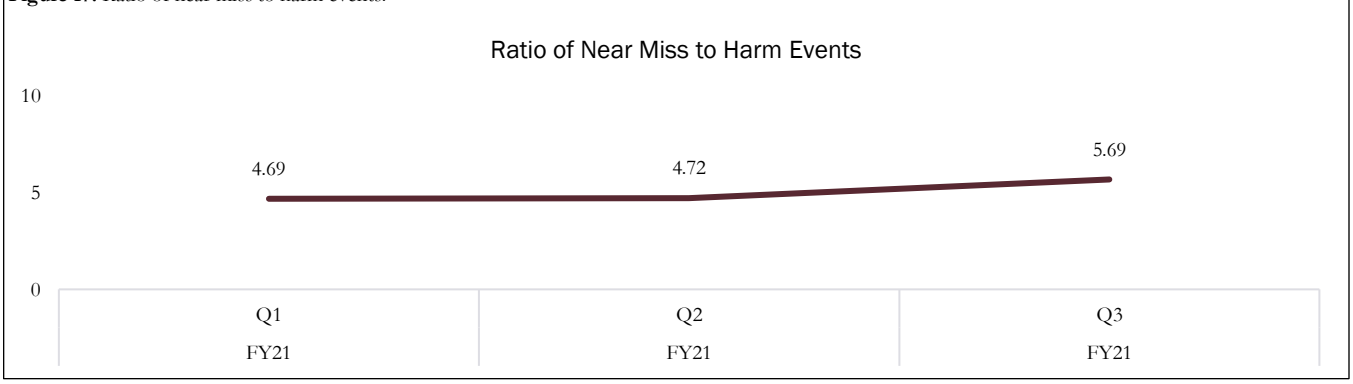
Figure 14 above visualizes self-reported health status (i.e., percent of respondents who rate their health as good, very good, or excellent) by quarter, which comes from the Joint Outpatient Experience Survey – Clinician and Group Consumer Assessment of Healthcare Providers and Systems (JOES-C). The survey is sent to all patients who visit an outpatient healthcare in either the direct or purchased care systems. Survey data lags approximately six months. Self-reported health metrics do not have an industry benchmark although both measures likely exceed the civilian population based on national trends in health-related quality of life. *Figure 15* above visualizes tobacco use rates by month. Data lags approximately three months. According to the triannual behavioral health survey of Active and Reserve forces, tobacco use is higher in the military population when compared to the civilian population.

Figure 16: Standard mortality ratio.



Healthcare effectiveness measured by the inpatient standard mortality ratio at MTFs as illustrated in *Figure 16* above**.** The MHS targets a value less than 1.0 for risk adjusted mortality, where a lower value indicates fewer observed deaths compared to expected deaths based on population characteristics. Standard mortality increased above 1.0 due to COVID-19 pandemic; COVID-19 diagnoses were not yet factored into the national mortality ratio expected deaths. Given the data lags associated with risk adjusted mortality, where the DoD relies on calculations from the Department of Health and Human Services (HHS), FY20 through FY21Q2 data is presented to identify current trends.

Figure 17: Ratio of near miss to harm events.



Safety and high reliability are measured by the total number of near miss events to total harm events expressed as a ratio as illustrated in *Figure 17* above. The ratio is balanced by the total number of harm events reported. Safety events are aggregated by quarter in accordance with 10 U.S.C. § 1102 *Confidentiality of medical quality assurance records: qualified immunity for participants*, to protect the identity of the patients. An increasing ratio demonstrates a greater willingness to report with less harm reaching the patient, both tenets of a highly reliable health service delivery organization. In the third quarter, the MHS experienced a total of 34,551 near miss events compared to 6,354 harm events.

The inpatient safety composite is currently disaggregated by MHS component. The Army (0.795), Navy (0.987), Air Force (0.729), and DHA (0.808) were all below the Department of Health and Human Services 1.000 threshold, indicating that fewer selected inpatient safety events were observed compared to expected in FY21 Q2.

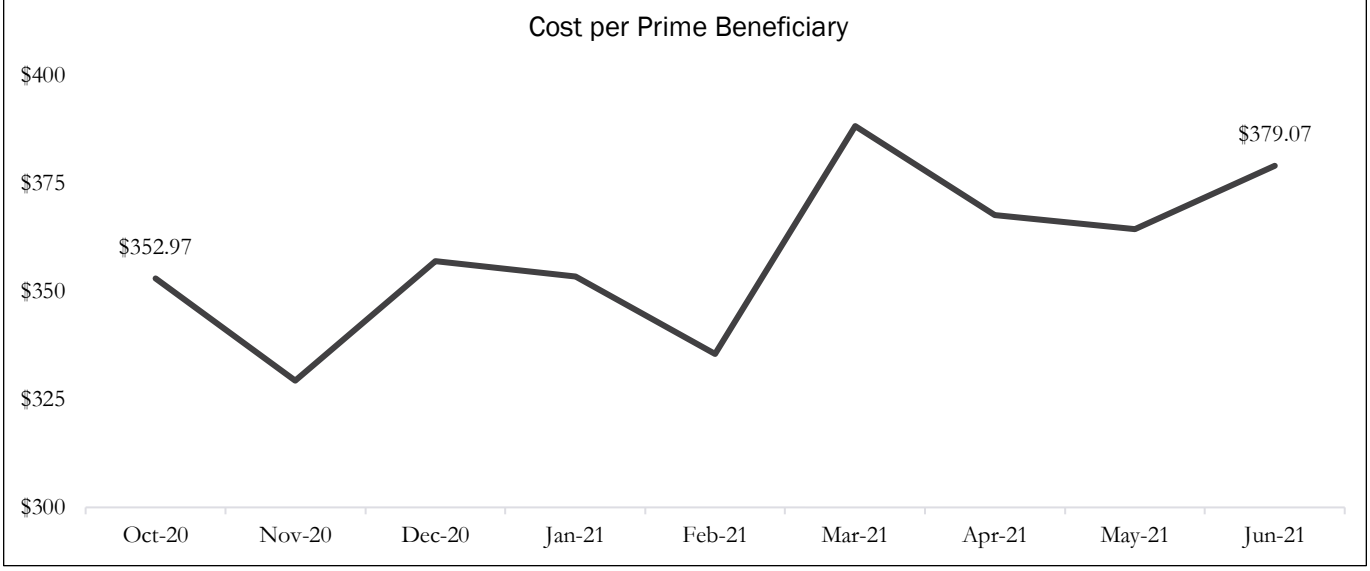
To assess satisfaction with the quality of care, TRICARE Inpatient Satisfaction Survey asks whether a patient recommends the MTF. DoD uses the same methodology as the Centers for Medicare and Medicaid Services' Hospital Consumer Assessment for Healthcare Providers and Systems (H-CAHPS) tool. This tool measures patients' perception of the quality of care provided. In FY21 Q1, 76.04% of respondents recommended the hospital. Data lags approximately nine months given the lags in coding and claims necessary to generate a patient's survey.

Goal 3: Reform the MHS for greater performance and affordability

There are six performance measures for goal three; three measures are currently available, and the remaining three are prototyped. These metrics measure efficiency of healthcare delivery and serve as an early warning system for financial management. Three measures available are: (1) cost per beneficiary for Health Maintenance Organization (HMO) (Prime); (2) total private sector care costs; and (3)

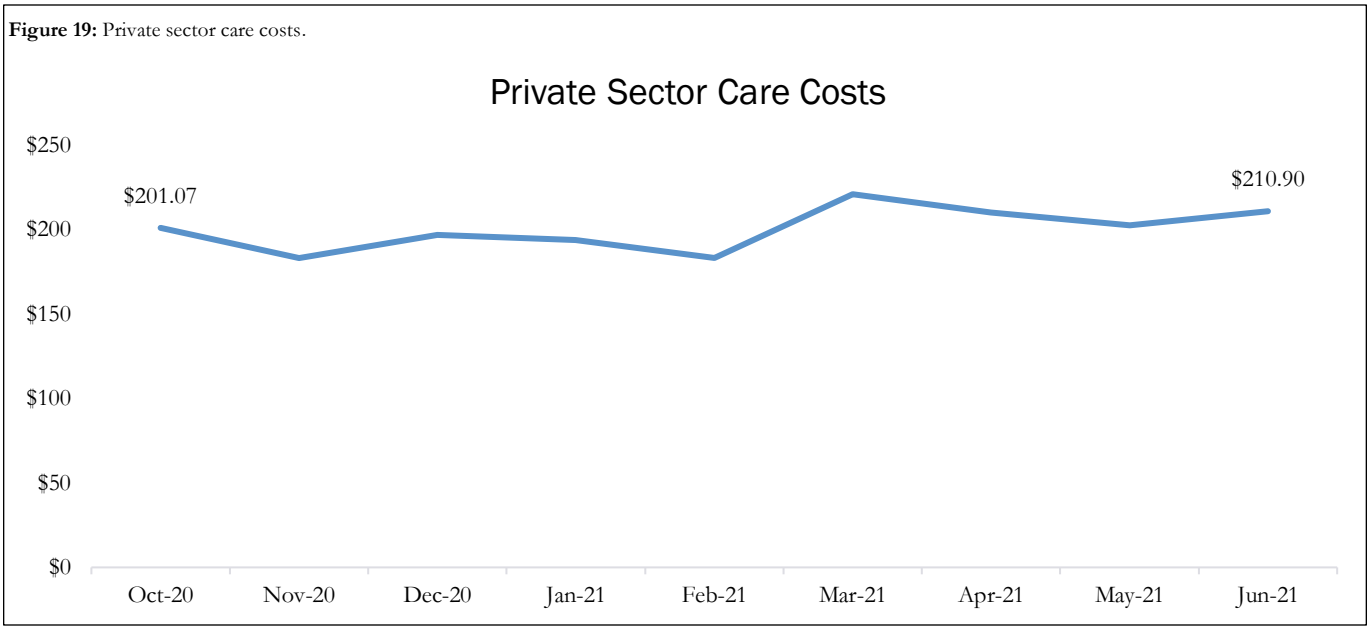
total enrollees to the MTFs. Three measures are prototyped: (1) cost per beneficiary for Preferred Provider Organization (PPO) (select); (2) cost per beneficiary for the Medicare-eligible population; and (3) deferrals from the MTFs to the private sector. Available full-time equivalent employees to the MTFs is still in development.

Figure 18: Cost per prime beneficiary.



Cost per beneficiary for Prime beneficiaries measures the relative efficiency of health service delivery at MTFs as illustrated in *Figure 18* above. The MHS uses the Kaiser Family Foundation annual rate of rise amongst U.S. payers as the target, which for FY 2021 is less than or equal to 4.50%. Due to the dramatic changes in health service delivery in light of the COVID-19 pandemic, cost per Prime beneficiaries grew 10.85%. Given the time required for generating, adjudicating, and paying claims for care referred out of the MTFs, data lags four months.

Figure 19: Private sector care costs.



Total private sector care cost measures the costs per Prime beneficiary for care outside of the MTF to identify costs that can be reduced through recapture as illustrated in *Figure 19* above. Costs decreased as care across the U.S. was deferred during the initial phase COVID-19 pandemic and quickly rebounded as healthcare organizations reopened. Like cost per Prime beneficiaries, data lags four months.

The MHS targets 3,003,704 TRICARE Prime enrollees for FY21. As of August 2021, the MHS reports 2,915,992 TRICARE Prime enrollees and 207,644 TRICARE Plus enrollees, for a total enrollment of 3,123,636 to the MTFs.

Analysis of Financial Statements and Stewardship Information

The financial statements of DHP reflect and evaluate the execution of its mission to provide a ready medical force and a medically ready force to Combatant Commands (CCMDs) in both peacetime and wartime. This analysis summarizes 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 financial statements include a consolidated balance sheets, 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. DHP also prepares a combining schedule of budgetary resources within required supplementary information.

Overview of Financial Position

Figure 20: Summary of DHP's major financial activities as of September 30, 2021 and 2020.

DHP Major Financial Activities *(dollars in thousands)*				
Net Financial Condition	FY 2021	FY 2020	$ Increase/(Decrease)	% Increase/(Decrease)
Fund Balance with Treasury	$ 20,458,873	$ 21,988,560	$ (1,529,687)	(7)%
Accounts Receivable, Net	949,738	1,036,901	($87,163)	(8)%
Inventory and Related Property and Other Assets	242,041	230,168	$11,873	5%
Property, Plant, and Equipment, Net	3,836,160	3,435,799	$400,361	12%
Advances and Prepayments	13,221	8,815	4,406	50%
Total Assets	**$ 25,500,033**	**$ 26,700,243**	**$ (1,200,210)**	**(4)%**
Accounts Payable	$ 1,251,263	$ 1,130,432	$ 120,831	11%
Federal Employee and Veteran Benefits Payable	259,167,054	272,588,380	(13,421,326)	(5)%
Environmental, Disposal Liabilities	19,633	18,378	1,255	7%
Other Liabilities	367,737	443,779	(76,042)	(17)%
Total Liabilities	**$ 260,805,687**	**$ 274,180,969**	**$ (13,375,282)**	**(5)%**
Unexpended Appropriations	$18,522,109	$ 20,210,255	$ (1,688,146)	(8)%
Cumulative Results of Operations	(253,827,763)	(267,690,981)	13,863,218	(5)%
Total Net Position	**$ (235,305,654)**	**$ (247,480,726)**	**$ 12,175,072**	**(5)%**
Net Program Cost	**$ 34,686,929**	**$ 38,921,409**	**$ (4,234,480)**	**(11)%**
Net Cost of Operations	**$ 21,723,925**	**$ 49,510,250**	**$ (27,786,325)**	**(56)%**
Budgetary Resources	**$ 45,031,849**	**$ 47,051,863**	**$ (2,020,014)**	**(4)%**

Preparing 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. DHA management is responsible for the integrity of the financial information presented in its financial statements. The DHA is committed to financial management excellence and is in process of developing and implementing a rigorous system of internal controls to safeguard its widely dispersed assets against loss from unauthorized acquisition, use, or disposition.

A summary of the DHA's major financial activities as of September 30, 2021, is presented in *Figure 20* 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 DHP, less earned revenue. Budgetary resources are funds available to DHP to incur obligations and fund operations.

Balance Sheets Summary

Assets – What We Own and Manage

Total assets were $25.5 billion as of September 30, 2021. The most significant assets are the Fund Balance with Treasury (FBwT) and Property, Plant, and Equipment, net, which represent a combined 95% of DHP's total assets. The largest, FBwT, consists of funds appropriated to DoD by Congress or transferred from other federal agencies and held in the U.S. Department of Treasury's accounts that are accessible to pay for DoD medical obligations. The FBwT decrease by $1.5 billion, or 7% is attributable primarily to decreases in funding provided by the *Coronavirus Aid, Relief, and Economic Security Act* (CARES Act). Additionally, the increase in Inventory and Related Property and Other Assets of $11.9 million, or 5%, is primarily attributable to stockpile materials at the BUMED, DHA and AFMS in the form of emergency supplies to be used in the event of a nationwide pandemic such as COVID-19.

Liabilities – What We Owe

Total liabilities of $260.8 billion as of September 30, 2021, of which $259.2 billion, or 99%, comprises federal employee and veteran benefits payable. These liabilities represent funds calculated by the DoD's Office of the Actuary (OACT) at the end of each FY using the current active and retired military population plus assumptions (inflation, discount rate, and medical trend) about future demographic and economic conditions. The 11% increase to accounts payable is due to factors including an increase in DHA's yearend accounts payable year accrual and net increases in payables for a variety of CRM programs. The decrease of $13.4 billion to Federal Employee and Veteran Benefits Payable is attributable to an overall decrease to DHP's actuarial liability.

Net Position – What We Have Done Over Time

Net position represents DHP's net results of activity over the years and includes unexpended appropriations and cumulative net earnings. 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, 2021, was ($235.3) billion. The decrease of $1.7 billion to unexpended appropriations was predominantly driven by a decrease in appropriations received by AFMS from FY 2020 to FY 2021. The change of $13.9 billion to cumulative results of operations is attributable to the overall change to DHP's unfunded actuarial liability.

Results of Program Cost

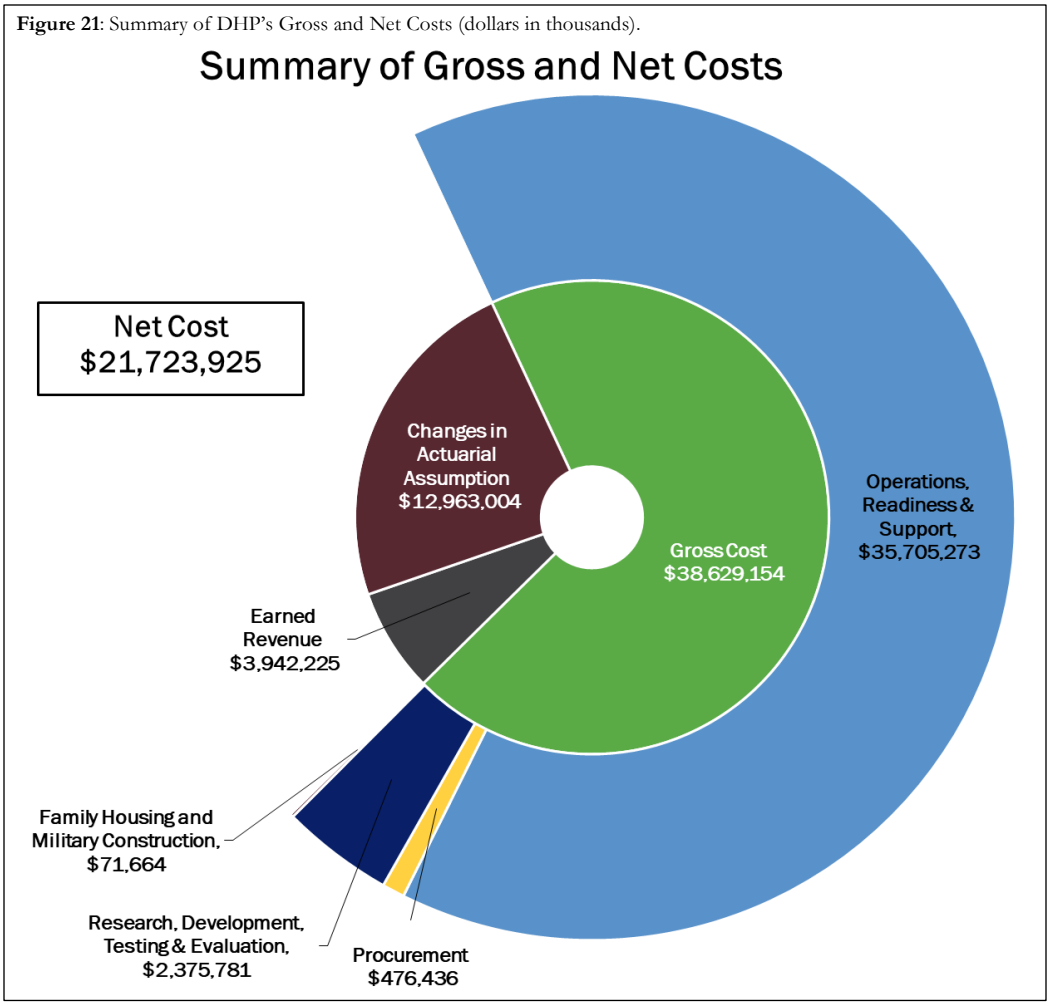
Net Costs – What Cost We Incurred for the Year

The net results of operations are reported in the consolidated SNC and the consolidated SCNP. The consolidated SNC represent the cost of operating (net of earned revenues) DHP's programs. In FY 2021, DHP operated the following four fund types:

- **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:** DHP appropriation procurement program funds acquisition of capital equipment in MTFs and other selected healthcare activities.
- **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 and 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 21 below shows a breakdown of the FY 2021 total net cost of operations of $21.7 billion to operate each of these DHP's programs. This is approximately a $27.8 billion decrease over FY 2020 in net costs mostly attributable to recognizing a gain from changes in actuarial assumption versus the loss recorded in FY 2020.

Figure 21: Summary of DHP's Gross and Net Costs (dollars in thousands).



Net Program costs represent the resources use by DHP to support the National Defense Strategy (NDS) and the three distinct lines of effort established for the DoD:

- Build a more lethal force
- Strengthen alliances and attract new partners
- Reform the Department for greater performance and affordability

The current enterprise strategy, released by the ASD(HA) in 2020, has three (3) goals for the MHS that focus on improvement and modernization:

- **Goal 1:** Measure and improve the readiness of the force
- **Goal 2:** Measure and improve health outcomes of the population we serve
- **Goal 3:** Reform the MHS for greater performance and affordability

The MHS strategy maintains alignment to the Quadruple Aim while providing more specific direction for the MHS components to ensure alignment to the NDS.

Measuring MHS performance is a means of improving program efficiency, effectiveness, and program results. One measure of MHS performance is the Department of Defense (DoD) *Evaluation of the TRICARE Program* Report[2] that is provided annually to Congress, as required per Section 717 of the P.L. 104-106 (NDAA for FY 1996). This report provides an assessment of the MHS overall performance in providing full-spectrum health care services to our 9.6 million Service member, retiree, and family member beneficiaries. The report includes both financial and non-financial measurements.

Additionally, the MHS tracks performance measures in support of each of the four key components of the Quadruple Aim. Information regarding these measures, methodology, and performance can be found by anyone with a CAC at *https://carepoint.health.mil*.

[2] *https://health.mil/Military-Health-Topics/Access-Cost-Quality-and-Safety/Health-Care-Program-Evaluation/Annual-Evaluation-of-the-TRICARE-Program*

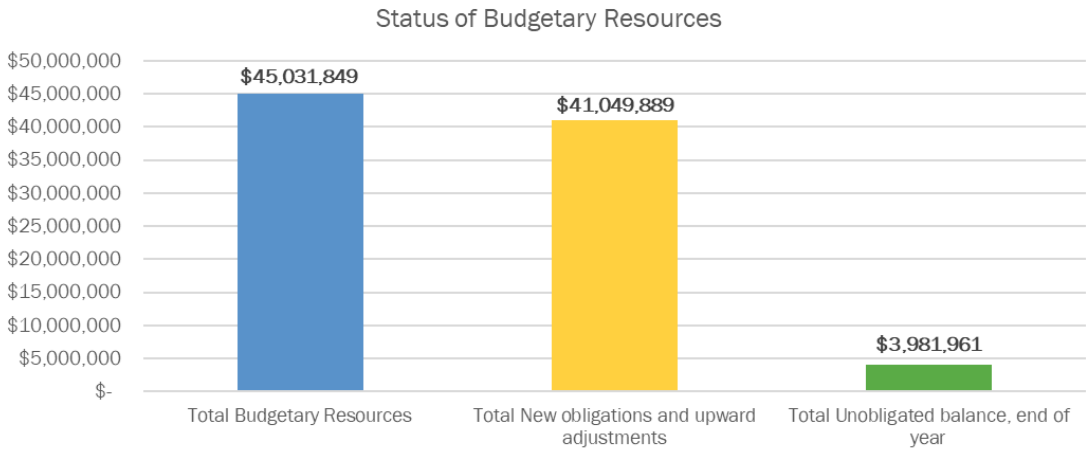
Budgetary Resources

Our Funds

The combined SBR provides information on the budgetary resources that were made available to DHP during the FY and the status of those resources at the end of the FY. 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 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 Medicare-Eligible Retiree Health Care Fund (MERHCF) Accrual Fund.

Figure 22 below shows the obligations incurred, unobligated balances, and total budgetary resources for DHP for as of September 30, 2021. DHP has received $45.0 billion in cumulative budgetary resources as of September 30, 2021, of which it has obligated $41.1 billion, to date.

Figure 22: Status of budgetary resources (dollars in thousands).



Obligations and Net Outlays

The status of budgetary resources shown above in *Figure 22* illustrates the overall total budgetary resources received and whether obligations were incurred, or the funding remains in unobligated balances on September 30, 2021. As shown in the chart, DHP's total budgetary resources as of September 30, 2021, was $45.0 billion. The net outlay for DHP as of September 30, 2021, is $35.5 billion.

Coronavirus Budgetary Resources

In December 2019, a novel strain of coronavirus was reported in Wuhan, China. The World Health Organization has declared the outbreak to constitute a "Public Health Emergency of International Concern." The President of the United States proclaimed that the COVID-19 outbreak in the United States constitutes a national emergency as of March 1, 2020. To address impacts of the virus on the Agency, the *Coronavirus Aid, Relief, and Economic Security (CARES) Act* was passed on March 27, 2020. This bill stated the funds received by the Agency for COVID-19 have the sole purpose of preventing, preparing for, and responding to coronavirus domestically or internationally. The *CARES Act* provided a total of $3.8 billion to the Agency to be used for COVID-19 activities within the Agency and its components. These funds are held centrally at DHA and distributed to the other DHP components. In addition, the *Families First Coronavirus Response Act* was passed on March 18, 2020. This bill provided $82 million to DHP for the purpose of providing health services consisting of SARS-CoV-2 or COVID-19 related items.

Current Fiscal Year Update

As of September 30, 2021, no additional funding has been allocated to DHP for the purpose of responding to the COVID-19 emergency. DHP continues to use the funds received under the *CARES Act* and *Families First Coronavirus Response Act* and expects these funds to remain available until September 30, 2022, or until all the funds are used, whichever occurs first. As of September 30, 2021, DHP had $223 million in unobligated COVID-19 related funding. While DHP did not receive additional COVID-19 related funding in FY 2021, it did redistribute COVID-19 related funding amongst its components. Additionally, certain DHP components deobligated COVID-19 related funding in FY 2021. Please see *Figures 23 and 24* below for more information regarding COVID-19 Funding for FYs 2020 and 2021.

Figure 23: Summarizes distributed and obligated resources for DHP as of September 30, 2021 for resources received for COVID-19 purposes.

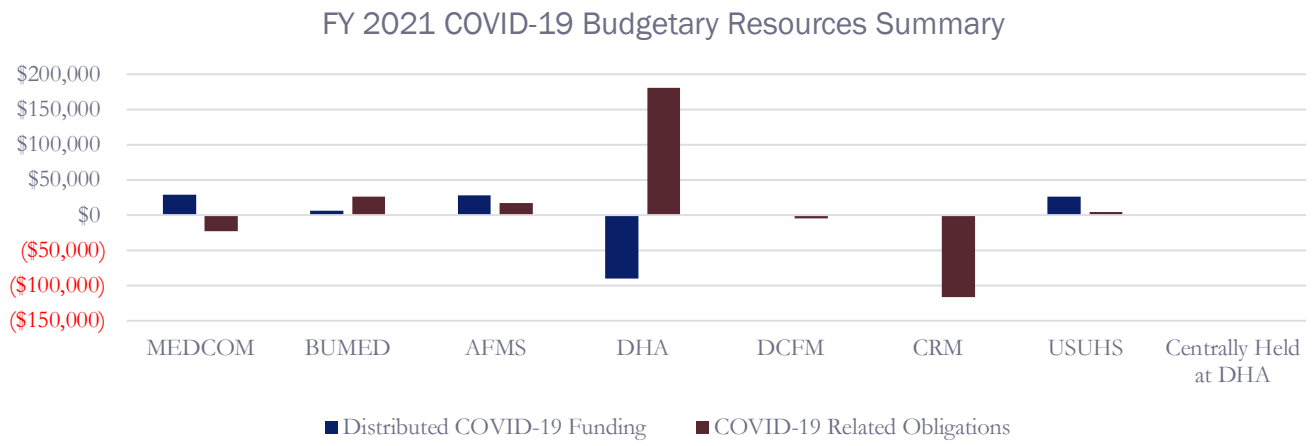
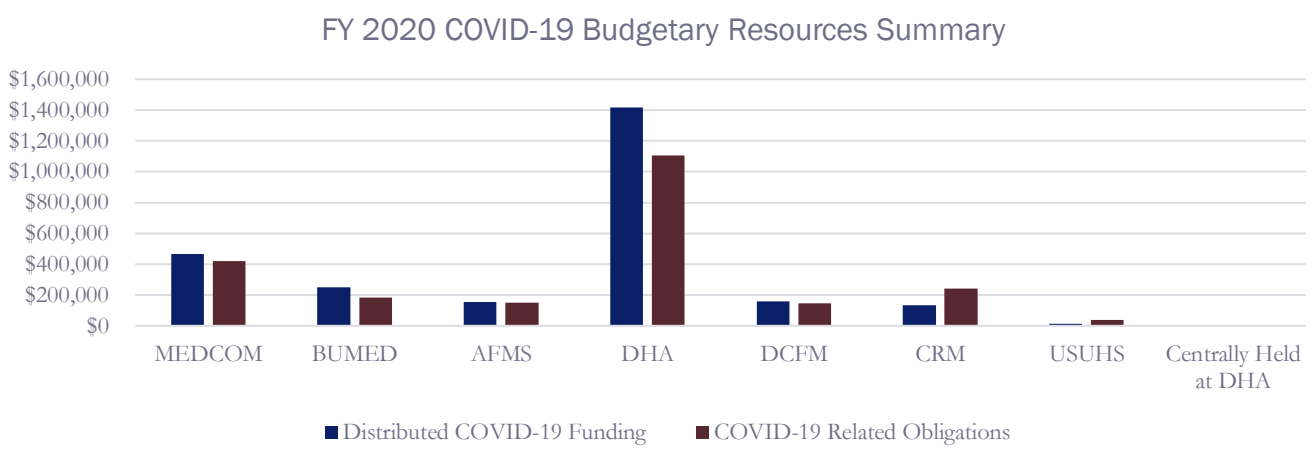


Figure 24: Summarizes distributed and obligated resources for DHP as of September 30, 2020 for resources received for COVID-19 purposes.



Limitations of the Financial Statements

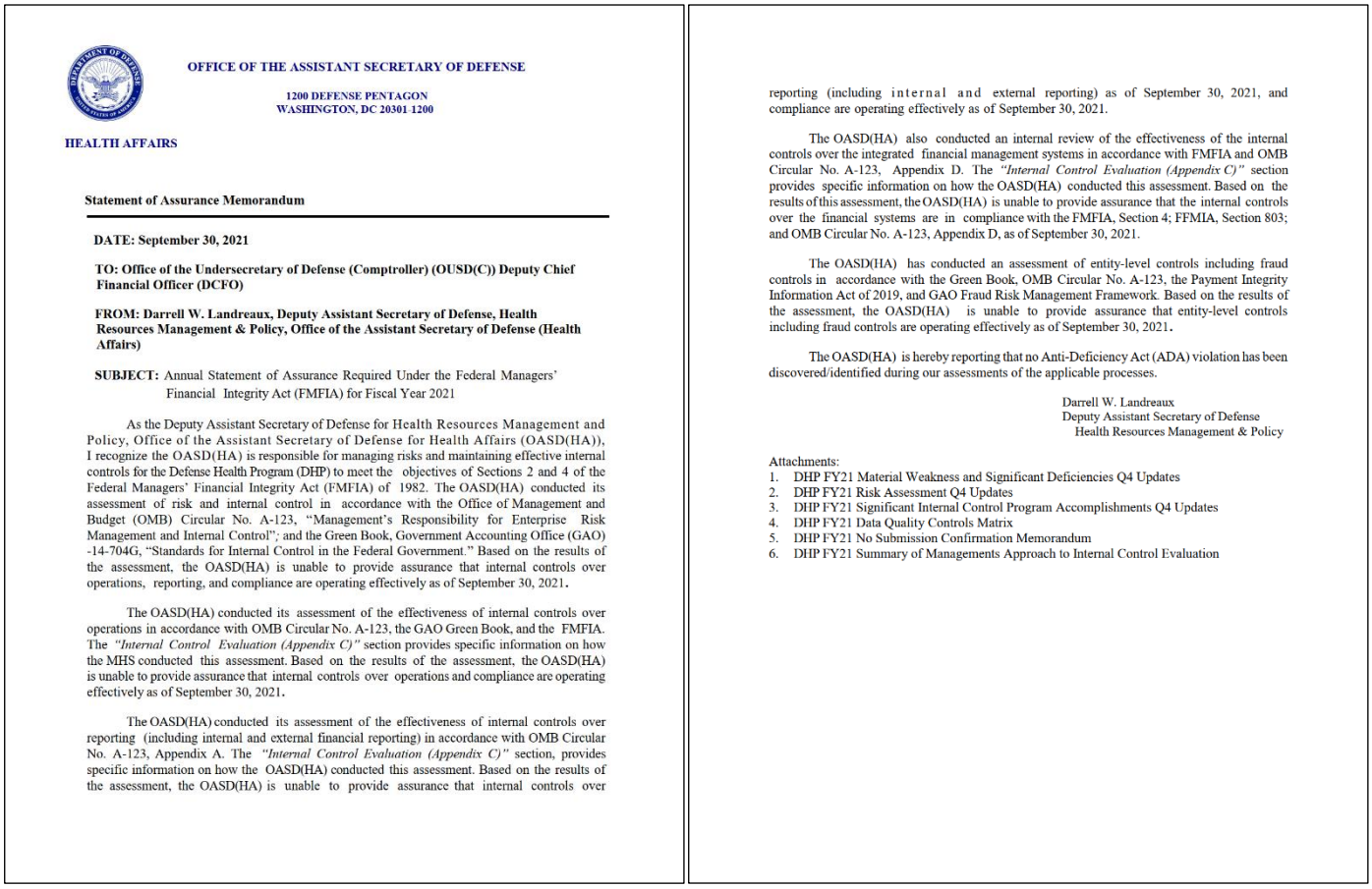
The principal financial statements are prepared to report the financial position, financial condition, and results of operations of DHP, pursuant to the requirements of *31 U.S.C. § 3515(b): Financial statements of agencies* (see USC note above). The statements are prepared from records of Federal entities in accordance with *Federal Generally Accepted Accounting Principles* (GAAP) and the formats prescribed by OMB. Reports used to monitor, and control budgetary resources are prepared from the same records. Users of the statements are advised that the statements are for a component of the U.S. Government.

Analysis of Systems, Controls, and Legal Compliance

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 Annual Statement of Assurance (SOA) below was provided for Federal Managers' Financial Integrity Act (FMFIA) for FY 2021.



OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE

1200 DEFENSE PENTAGON
WASHINGTON, DC 20301 1200

HEALTH AFFAIRS

Statement of Assurance Memorandum

DATE: September 30, 2021

TO: Office of the Undersecretary of Defense (Comptroller) (OUSD(C)) Deputy Chief Financial Officer (DCFO)

FROM: Darrell W. Landreaux, Deputy Assistant Secretary of Defense, Health Resources Management & Policy, Office of the Assistant Secretary of Defense (Health Affairs)

SUBJECT: Annual Statement of Assurance Required Under the Federal Managers' Financial Integrity Act (FMFIA) for Fiscal Year 2021

As the Deputy Assistant Secretary of Defense for Health Resources Management and Policy, Office of the Assistant Secretary of Defense for Health Affairs (OASD(HA)), I recognize the OASD(HA) is responsible for managing risks and maintaining effective internal controls for the Defense Health Program (DHP) to meet the objectives of Sections 2 and 4 of the Federal Managers' Financial Integrity Act (FMFIA) of 1982. The OASD(HA) conducted its assessment of risk and internal control in accordance with the Office of Management and Budget (OMB) Circular No. A-123, "Management's Responsibility for Enterprise Risk Management and Internal Control"; and the Green Book, Government Accounting Office (GAO) -14-704G, "Standards for Internal Control in the Federal Government." Based on the results of the assessment, the OASD(HA) is unable to provide assurance that internal controls over operations, reporting, and compliance are operating effectively as of September 30, 2021.

The OASD(HA) 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 MHS conducted this assessment. Based on the results of the assessment, the OASD(HA) is unable to provide assurance that internal controls over operations and compliance are operating effectively as of September 30, 2021.

The OASD(HA) 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 OASD(HA) conducted this assessment. Based on the results of the assessment, the OASD(HA) is unable to provide assurance that internal controls over reporting (including internal and external reporting) as of September 30, 2021, and compliance are operating effectively as of September 30, 2021.

The OASD(HA) 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 OASD(HA) conducted this assessment. Based on the results of this assessment, the OASD(HA) 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 30, 2021.

The OASD(HA) has conducted an assessment of entity-level controls including fraud controls in accordance with the Green Book, OMB Circular No. A-123, the Payment Integrity Information Act of 2019, and GAO Fraud Risk Management Framework. Based on the results of the assessment, the OASD(HA) is unable to provide assurance that entity-level controls including fraud controls are operating effectively as of September 30, 2021.

The OASD(HA) is hereby reporting that no Anti-Deficiency Act (ADA) violation has been discovered/identified during our assessments of the applicable processes.

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

Attachments:
1. DHP FY21 Material Weakness and Significant Deficiencies Q4 Updates
2. DHP FY21 Risk Assessment Q4 Updates
3. DHP FY21 Significant Internal Control Program Accomplishments Q4 Updates
4. DHP FY21 Data Quality Controls Matrix
5. DHP FY21 No Submission Confirmation Memorandum
6. DHP FY21 Summary of Managements Approach to Internal Control Evaluation

Summary of Internal Control Assessment

DHP conducted its assessment of the effectiveness of ICO in accordance with the *FMFIA* and the *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 DHP with the results and testing methodology used to evaluate the status of the control. Based on the results of the assessment, DHP is unable to provide assurance regarding the effectiveness of our ICO as of September 30, 2021.

DHP assessed the effectiveness of Internal Controls Over Financial Reporting-Financial Reporting (ICOFR-FR), 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 DHP with the results and testing methodology used to evaluate the status of the control. Based on the results of the assessment, DHP is unable to provide assurance that ICOFR-FR were operating effectively as of September 30, 2021.

DHP also conducted an internal review of the effectiveness of Internal Controls Over Reporting Financial Systems (ICOFR-FS) in accordance with *FFMIA of 1996* (P. L. 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, DHP is unable to provide assurance that the internal controls over the financial systems are in compliance with the *FMFIA* and *OMB Circular No. A-123, Appendix D*, *Compliance with the Federal Financial Management Improvement Act (FFMIA) of 1996* as of September 30, 2021.

Material weaknesses were also identified in the following areas as a result of the financial statement audit:

- Accounting and Financial Reporting Governance Structure, Entity-Level Controls
- Financial Reporting – Universe of Transaction Reconciliations
- Financial Reporting – Defense Departmental Reporting System Adjustments
- Fund Balance with Treasury
- Medical Revenue and Associated Receivables
- General Equipment Existence and Completeness
- Valuation of Property, Plant, and Equipment
- Stockpile Materials
- Liabilities and Related Expenses
- Monitoring and Reporting of Obligations and Adjustments
- Information Systems

DHP Risk Management Internal Control Program is focused on refining and improving the Entity Level Controls (ELCs) moving into FY 2022. Correcting design failures and strengthening the ELCs should help DHP 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 2021 financial statement audit. Our auditor has noted DHP financial management systems did not comply with the (1) federal financial management system's requirements, (2) applicable federal accounting standards promulgated by Federal Accounting Standards Advisory Board (FASAB), and (3) 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. DHP continues to develop a series of reconciliations that ties the General Ledger (GL) details from its different accounting systems to the financial statements. As a result, DHP was able to support some of the financial statement line items down to the supporting GL system detail. DHP continues the process of evaluating the FY 2021 audit findings contributing to noncompliance to continue 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. 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 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 (PPA) (P. L. 97-177), 31 U.S.C. §§ 3901–3907

In 1982, Congress enacted the *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 (WAWF)) 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, P. L. 104-134), 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.

DHA in coordination with DHA Office of General Counsel (OGC) are in the process of implementing a Debt Adjudication process for FY 2022 to address the FY 2019 MEDCOM reported material weakness on Medical Delinquent Debt Management; (a) lack of compliance with financial regulations with respect to debt management, including requirements associated with transfer of debt, timeliness, and debt assignment, and (b) information systems support for Uniform Business Office (UBO) processes. The process will determine what patient debt may be suspended, compromised, or terminated in accordance with current Federal Statutes and Financial Management Regulation (FMR).

Government Charge Card Abuse Prevention Act of 2012 (P. L. 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 OIG 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 of 2014 (FISMA, P.L. 113-283)

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 2021 DHP was not in compliance with *FISMA* due to the several identified deviations from National Institute of Standards and Technology (NIST) standards and guidelines.

Federal Financial Management Improvement Act of 1996 (FFMIA, P.L. 104-208)

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

In FY 2021 DHP's financial management systems did not substantially comply with the requirements within *FFMIA*, as asserted to by management due to the asserted departures from *GAAP* and *USSGL* requirements.

Federal Managers' Financial Integrity Act of 1982 (FMFIA, P.L. 97-255)

The *FMFIA* requires agencies to establish and maintain internal control and financial management systems to provide reasonable assurance that the three objectives of internal control: 1) effectiveness and efficiency of operations, 2) compliance with applicable laws and regulations, and 3) reliability of financial reporting are achieved.

In FY 2021 DHP's financial management systems did not substantially comply with the requirements within *FMFIA*, as asserted to by management due to the lack of establishment and implementation of controls as detailed in the SOA.

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 (DATA Act, P. L. 113-101)

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 2020 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*.

DHP does not have a Data Quality Plan in place for FY 2021 and will begin the assessment and implementation process in FY 2022.

Grants Oversight and New Efficiency Act (P. L. 114-117)

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.

In FY 2021 DHP did not to evaluate the compliance requirements within *GONE Act*.

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

Title 10, U.S.C., § 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 *NDAA* for FY 2017 has called for the reform of the MHS and MTFs. According to Section 702 of the *NDAA* for FY 2017, "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 DHP appropriation is undergoing audit as a single entity. To adhere to the *NDAA* for FY 2017, 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 *NDAA* for FY 2017 compliance strategy is being executed by using a single accounting solution, General Fund Enterprise Business System (GFEBS). This Commercial Off-the-Shelf (COTS) Enterprise Resource Planning (ERP) software tool built by Systems Applications and Products (SAP), and 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 the current MHS adopters, and in turn better accountability of our funds. GFEBS is a modern ERP with inherent commercially available "best practices" and is actively maintained and updated by its provider. GFEBS also provides analytical data and tools, reduces the cost of business operations through industry-tested efficiencies, and improves comparability of Service Components. In time, use of the system will enable DHP to meet congressional mandates, requiring audit compliance and an accurate accounting of all financial transactions. Army received an adverse opinion on the GFEBS System and Organization Controls (SOC) 1 report in 2021. The mitigation strategies and way ahead on corrective actions are in active coordination and discussion.

MEDCOM implemented GFEBS in FY 2010, and in FY 2015, a proof-of-concept GFEBS deployment to the National Capital Region Medical Directorate (NCR MD), now under the DHA, to include Walter Reed National Military Medical Center (WRNMMC). 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 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 DHP funding on GFEBS.

DHA and USUHS deployed GFEBS on April 2, 2018, and the BUMED transition began in FY 2019 and was originally planned with a four-wave deployment schedule. BUMED deployed GFEBS at various times throughout FY 2020, with the final, Wave 3B, deploying on August 3, 2020. The BUMED deployment was completed on schedule for all Navy MTFs. For all the previous deployments the ASD(HA) has agreed to deploy GFEBS "as-is" with basic Army functionality.

On May 8, 2020, BUMED Leadership unilaterally decided that all non-MTFs except for DHP Funded Navy Medicine Readiness and Training Commands would no longer transition to GFEBS. This decision effectively canceled all of Wave 4 deployment, as Wave 4 consisted of Navy Labs. Beginning in FY 2021, DHP now has over 80% of funds, excluding CRM, going through GFEBS.

Additionally, the ASD(HA) sponsored an assessment of deploying GFEBS to AFMS. The assessment identified 13 risks/challenges in three categories (technology, operations and change management) to address prior to deploying GFEBS to AFMS. The assessment concluded that GFEBS implementation at AFMS is achievable. The final report was coordinated with Senior Leadership in ASD(HA), DHA, AFMS, GFEBS Project Management Office (PMO) and Deputy Assistant Secretary of the Army Financial Information Management (DASA FIM). On August 24, 2020 the ASD(HA) submitted an official request to the Army for the fielding of GFEBS at AFMS. On September 28, 2020, the Army responded favorably to the request. The MHS will leverage the existing support function to begin working considerations through the Army Technical Financial Information Council (tFIC) for the fielding of GFEBS to the AFMS. The ASD(HA) has begun working with AFMS and the Army counterparts on pre-deployment planning activities to include finalizing the Business Justification Form that will be vetted through the Army Governance process. Upon completion of Army's Systems Integrator transition by the end of December 2021, the Army and MHS will begin final planning activities for an AFMS GFEBS deployment.

In addition to GFEBS, DHP utilizes the following General Ledger (GL) systems: Defense Agencies Initiative (DAI), 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). Upon GFEBS implementation for DHA and BUMED, DAI and STARS-FL will brown out over a five-year period in conjunction with their go-live dates.

DEAMS is a Major Automated Information System (MAIS) that uses COTS ERP software to provide accounting and management services for the AFMS. 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 Defense Finance and Accounting Service (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. At the end of FY 2021, the Department of Navy and DFAS plans to terminate STARS-FL.

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), CHCS, and Defense Medical Logistics Standard Support (DMLSS). DHA also relies on service provider feeder systems. For service provider systems, DHP obtains 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 *NDAA* for FY 2017's intent in driving 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 new Army Governance councils, the tFIC. These new councils replace the Army GFEBS Functional Governance Board (FGB) for requesting system enhancements, and the Army GFEBS Process Owners Group (POG). Furthermore, the "one voice" concept applies to audit support requests and other requests for information or updates to and 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, 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 DHP per the *NDAA* for FY 2017 will now be represented by the ASD(HA)'s designated department defined below.

In a concerted effort to consolidate the varying voices of MHS into a single, focused entity, ASD(HA) previously stood up the Health Affairs Functional Champion (HAFC) to represent the MHS in the Army Governance structure and to standardize business processes within GFEBS. The HAFC has stood up the MHS GFEBS Governance Board (GGB) to review and adjudicate system enhancement requests and business process standardization issues. Chaired by the HAFC Director, the MHS GGB is comprised of voting members of all the MHS Components. To assist the GGB voting members with the assessment and deliberation of GFEBS related issues, two subordinate workgroups have been established, with representation from all the MHS Components, the MHS GFEBS System Change Group (SCG), which focuses on GFEBS system enhancements, and the Business Process Standardization and Policy (BPSP), which focuses on standardizing GFEBS related business processes across the entire MHS.

Prior to the escalation of issues to Army's tFIC for official consideration, the SCG and GGB identify, validate, and set priorities for GFEBS enhancements requested by the MHS. This process will identify MHS priorities while also highlighting audit compliance and cost savings/avoidance where applicable.

This consolidation of MHS as required by the *NDAA* for FY 2017 will strengthen the 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 organize clearly and effectively, 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.

RevX Overview

The Revenue Cycle Expansion Project, or RevX, refers to a collection of capabilities within MHS GENESIS, and is projected to be implemented February 2022. This implementation will include multiple capabilities that will replace current DHA financially relevant feeder systems, such as ABACUS and CCE. ABACUS, which is strictly a billing system, will be replaced by the Cerner Patient Accounting Module (CPAM) which is a patient-level accounting system allowing for the capture of itemized cost of care for every medical service or product within an encounter, through the utilization of an embedded DoD-specific charge description master. CCE will be replaced by another 3M™ product called 3M™ 360 Encompass™, which will include a natural language processor and auto-suggested coding.

These capabilities will provide greater visibility of cost at the patient level and advance the auditability of the MHS. Naval Hospital Bremerton and Naval Health Clinic Oak Harbor were identified as the initial sites to receive RevX. The remaining sites already on MHS GENESIS will receive RevX in Wave Groups and those sites beginning with Waves Gordon-Beaumont will receive RevX as part of the MHS GENESIS baseline.

Additional RevX capabilities include:

- Other Health Insurance discovery through Experian Health;
- Allows for Prior Authorization procedures to be implemented and standardized;
- Patient Identification Process (PIP) (replacing Patient Categories) including the selection of a patient profile and health plan at the point of scheduling with verification at registration/check-in. Interim PIP will be operational for all facilities on MHS GENESIS in February 2022 while the final PIP implementation is to be determined (TBD);
- Automated Current Procedural Terminology (CPT), Healthcare Common Procedure Coding System (HCPCS), charge and workload capture based on clinician orders and documentation;
- Charge accrual for all encounters;
- Improved referral processes to enable care coordination with our Managed Care Support Contractors (MCSC) and Veterans Health Administration (VHA) partners;
- Pharmaceutical claims processing at the point of dispensing through the PharmNet application (implementation TBD);
- Alpha II, an integrated claims scrubber to improve data quality and reduce the probability of denied claims;
- Automated claims generation for encounters cleanly passing through Alpha II;
- SSI Clearinghouse to facilitate transmission of claims to the appropriate third-party insurer;
- Improved accounts receivable and denials management tracking through standardized workflows and work queues;
- Interface between CPAM and GFEBS (implementation TBD);
- Patient Statements vendor, RevSpring, to assist Uniform Business Office staff in directly billing self-pay beneficiaries; and
- Improved revenue cycle reports through HealtheIntent/HealtheAnalytics.

Along with RevX implementation a complete review of revenue cycle policies and procedures will be conducted and updated as required. Standard operating procedures will be developed for scheduling and registration including the new PIP processes, referral management, coding, and billing. Standardized workflows are also being developed to help manage beneficiaries accessing both DoD and the VHA systems to improve documentation and resulting billing processes. Successful outcomes are dependent on a commitment from every MHS GENESIS end-user to adopt the new system and updated procedures, implementation of an effective training approach, and revenue cycle maintenance procedures and internal sustainment structure to continuously improve the system. Overall end-users can expect:

- Standardized business processes and workflows across all MTFs;
- Integrated communication between the business and clinical communities;
- Interagency interoperability resulting from use of vendor model standards;
- Access to industry standard reports with the ability to adjust report filters and parameters;
- Ability to support audit readiness through detailed resource allocation; and
- Targeted work queues so staff can work outstanding accounts based on priorities.

Forward-Looking Information

Our FY 2022 DHP (DHP) budget request presents a balanced, comprehensive strategy that aligns with the Secretary of Defense's priorities to (1) defend the nation; (2) take care of our people; and (3) succeed through teamwork. It includes funding for the Department's ongoing efforts to eradicate the coronavirus 2019 (COVID-19) virus and invests in future modernization, while preserving present readiness to cement our status as the best joint fighting force in the world.

The MHS remains committed to our priority of defending the nation. We will continue to act boldly and quickly to support Federal and state efforts to defeat COVID-19 for as long as it remains a threat. In FY 2021, the most significant COVID-19-related costs to DHP stemmed from higher than projected CRM costs; additional laboratory testing; personal protective equipment expenditures; and numerous other requirements—from public health surveillance to antiseptic cleaning of MTFs. As variants emerge, we must remain vigilant and maintain a heightened awareness of unanticipated, notable expenditure trends that deviate from programmed budgets and spend plans.

As we implement the transition of MTFs to the Defense Health Agency's (DHA's) management per the Department's approved, conditions-based execution plan, the FY 2022 budget request reflects our focus on additional business reforms and process standardizations to ensure projected savings stemming from the transition are realized. The DHA's centralized administration of MTFs will transform the MHS into an integrated readiness and health system, eliminate redundancies, and create a standardized high quality care experience for our beneficiaries.

In FY 2022, DHP budget request for CRM represents roughly half of DHP O&M budget. Over the period of FY 2012 to FY 2018, both private health insurance premiums and National Health Expenditures (NHE) per capita rose about 3.7% annually. Although the CRM budget should have increased accordingly, the Department instituted a series of initiatives that averted cost increases. In FY 2020, the COVID-19 pandemic significantly reduced the utilization of healthcare services. In FY 2021, we saw costs move to more normal (pre-pandemic) levels, and then spike upwards. As the pandemic continues, CRM costs must be monitored closely.

Our FY 2022 DHP Operation and Maintenance (O&M) budget request reflects myriad initiatives, some of which are:

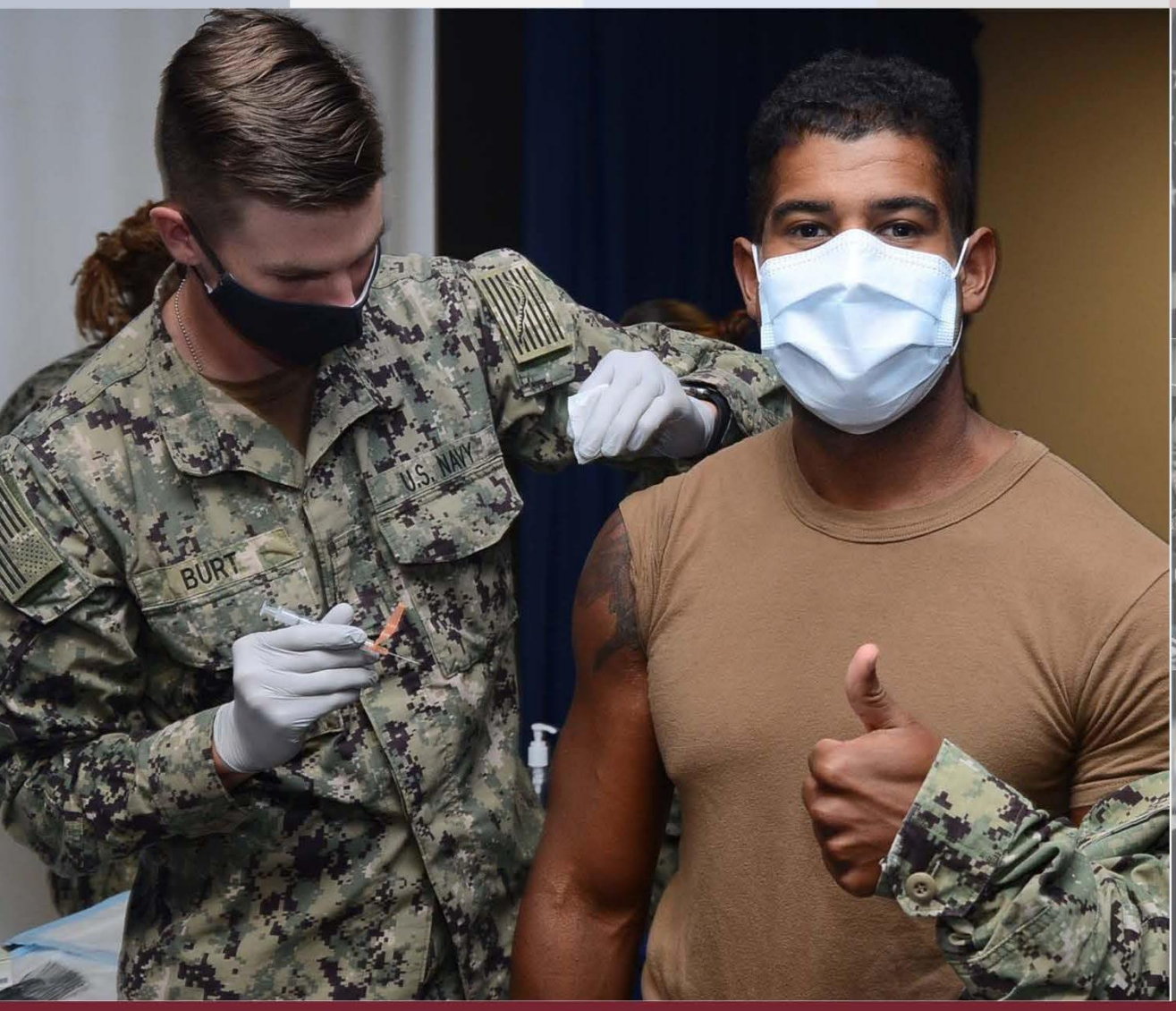
- Establishing a Medical Logistics Enterprise Activity to leverage best practices and limit variation in logistical support to MTFs for non-drug supplies, equipment, and services.
- Funding the clinical application, HealtheIntent, which provides a platform for population health and analytic tools and offers a seamless longitudinal record between the Department and the Department of Veteran Affairs.
- Expansion of MHS GENESIS to San Antonio Military Medical Center, Joint Base San Antonio, Fort Hood, Texas, Fort Bragg, North Carolina, William Beaumont Army Medical Center, Fort Gordon, Georgia, Naval Hospital Jacksonville, and Eglin Air Force Base.
- Deployment of RevX (the accounting system for MHS GENESIS) to all facilities that have, or will have, MHS GENESIS deployed during FY 2022.
- Increase of $191.4M to the CRM baseline attributed to the NHE inflationary growth.
- Funding of $146.6M for Public Health Surveillance, for expanded contact tracing, testing, and screening and continued efforts to identify variants to prevent the further spread of COVID-19.
- Funding of $104.5M for civilian full-time equivalents (FTEs) and contractor FTEs to ensure uninterrupted access to timely, high-quality healthcare as the Department redirects uniformed manpower toward more direct warfighting functions.
- Funding of $66.6M for MTF and DHA Information Management/Technology.
- Funding of $39.1M for civilian personnel awards.
- Funding of $37M for increases to pharmaceutical requirements.

Some of the initiatives contained within the FY 2022 DHP Procurement budget request includes investments in the radiographic, surgical, and information systems functional areas, which are driven by rapid technological advancements and the need for the MHS to maintain the standards of care set by the civilian healthcare sector. Our procurement budget also funds the new facility outfitting program element designed to furnish new and expanded Military Construction projects with pathologic, dental, surgical, and administrative equipment in support of dental and healthcare services.

The goal of our DHP research, development, test, and evaluation (RDT&E) efforts are to advance the state of medical science in those areas of most pressing need and relevance to today's battlefield experience and emerging threats. Some of the initiatives in our FY 2022 DHP RDT&E budget request reflects funding for joint battlefield healthcare, and military health and recovery aimed at injury

prevention and recovery related to blunt, blast, and accelerative and musculoskeletal injuries. It also includes funding for studies in bacterial diseases and treatment of infections with multi-drug resistant bacterial pathogens; as well as emerging infectious and acute respiratory diseases. In the coming years, we hope to leverage new technologies to include artificial intelligence and machine learning, biotechnology, and autonomous systems.

As we enter our fifth year of DHP financial statement audits, we are on an irreversible path to remediate audit findings and to strengthen our internal controls. We have made significant strides to comply with accounting principles and policies, and to overcome accounting system limitations. While a great deal of work remains to be done, we have an incredible cadre of medical resource managers, budget analysts, and accountants, with drive, skill, and commitment to advancing our remediation efforts toward the goal of a clean audit opinion.



Financial Information

Section II

Defense Health Program

Office of the Inspector General Transmittal

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

November 8, 2021

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 Financial Statements and Related Notes for FY 2021 and FY 2020 (Project No. D2021-D000FT-0055.000, Report No. DODIG-2022-015)

We contracted with the independent public accounting firm of Kearney & Company to audit the Defense Health Program (DHP) Financial Statements and related notes as of and for the fiscal years ended September 30, 2021, and 2020. The contract required Kearney & Company to provide a report on internal control over financial reporting and compliance with provisions of applicable laws and regulations, contracts, and grant agreements, and to report on whether the DHP's financial management systems substantially complied with the requirements of the Federal Financial Management Improvement Act of 1996. 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, Volume 1 (Updated, April 2020), Volume 2 (Updated, March 2021), and Volume 3 (Updated, September 2021). 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 FY 2021 and FY 2020 Financial Statements and related notes.

Kearney & Company's separate report, "Independent Auditor's Report on Internal Control Over Financial Reporting," discusses 11 material weaknesses related to the DHP's internal controls over financial reporting.* Specifically, Kearney & Company's report concluded that the DHP did not:

- implement an effective oversight structure to monitor accounting and financial reporting of DHP Components or meet the standards for an effective internal control system;
- maintain effective controls to ensure that the universe of transactions reconciliation process was complete and supported;
- fully support adjustments processed and recorded during the quarterly financial statement compilation process;
- develop sufficient policies, procedures, and internal controls to fully reconcile Fund Balance With Treasury;
- account for revenue and accounts receivable in accordance with Generally Accepted Accounting Principles or accurately account for revenue and accounts receivable due to ineffective medical coding procedures;
- design and implement policies, procedures, and controls to appropriately and accurately report general equipment;
- value Property, Plant, and Equipment in accordance with Generally Accepted Accounting Principles;
- report stockpile materials in accordance with Generally Accepted Accounting Principles;
- establish a process to record liabilities and related expenses completely and accurately;
- validate and accurately report obligation activity; and
- ensure the effective design and operation of financial information systems.

* 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.

Kearney & Company's additional report, "Independent Auditor's Report on Compliance With Laws, Regulations, Contracts, and Grant Agreements," discusses five instances of noncompliance with provisions of applicable laws and regulations, contracts and grant agreements, and potential violations of the Antideficiency Act. Specifically, Kearney & Company's report describes instances in which the DHP did not comply with the Federal Managers' Financial Integrity Act of 1982, the Federal Information Security Modernization Act of 2014, the Federal Financial Management Improvement Act of 1996, the Debt Collection Improvement Act of 1996, and the Prompt Payment 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 and related notes in accordance with GAGAS, was not intended to enable us to express, and we do not express, an opinion on the DHP FY 2021 and FY 2020 Financial Statements and related notes. Furthermore, we do not express conclusions on the effectiveness of internal control over financial reporting, on whether the DHP's financial systems substantially complied with Federal Financial Management Improvement Act of 1996 requirements, or on compliance with provisions of applicable laws and regulations, contracts, and grant agreements. Our review disclosed no instances where Kearney & Company did not comply, in all material respects, with GAGAS. Kearney & Company is responsible for the attached November 8, 2021 reports, and the conclusions expressed within the reports.

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

Lorin T. Venable

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, 2021 and 2020, 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. 21-04, *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, *Summary of 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:

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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 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*
- Accounting and reporting requirements associated with SFFAS No. 31, *Fiduciary Activities*
- 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*
- Recognition and valuation requirements set forth in SFFAS No. 44, *Accounting for Impairment of General Property, Plant and Equipment Remaining in Use*
- Accounting and reporting requirements associated with restatements per SFFAS No. 21, *Reporting Corrections of Errors and Changes in Accounting Principles*, and OMB Circular A-136, *Financial Reporting Requirements*

We were unable to obtain sufficient appropriate evidential matter as to the completeness of the financial statements reported as of September 30, 2021. This includes $20.5 billion of Fund Balance with Treasury (FBWT), $1.3 billion of Accounts Payable (AP) ($100.3 million Federal and $1.2 billion Non-Federal), and $367.7 million in Other Liabilities ($96.2 million Federal and $271.5 million Non-Federal) 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 (GL) reporting requirements. The DHP is unable to reconcile its financial statements to supporting 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 (I&RP) line item of the Balance Sheet. As of September 30, 2021, the DHP reported approximately $242.0 million of I&RP on the Balance Sheet, consisting solely of

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stockpile material. The DHP did not record stockpile material in accordance with 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.

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, 2020 or ending balance balances as of September 30, 2021 were free of material misstatements. Our work identified issues related to existence, completeness, valuation, and disclosure of Construction-in-Progress (CIP), Internal Use Software (IUS) (including IUS in development), and General Equipment. As of September 30, 2021, the DHP reported $3.8 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 (AR). The DHP does not account for all revenue and AR transactions using the accrual basis of accounting, recording certain activity on the cash basis of accounting. As of September 30, 2021, the DHP reported $949.8 million of AR ($206.1 million Federal and $743.7 million Non-Federal), net on its Balance Sheet and $3.9 billion of earned revenue on its Statement of Net Cost.

We were unable to obtain sufficient appropriate audit evidence to support the existence and accuracy of Gross Costs. For the period ended September 30, 2021, the DHP reported $38.6 billion in Gross Costs on its Statement of Net Cost.

We were unable to obtain sufficient appropriate audit evidence to support the accuracy and completeness of Unobligated balance from prior-year budget authority, net. As of September 30, 2021, the DHP reported $6.0 billion of Unobligated balance from prior-year budget authority, net on its Statement of Budgetary Resources.

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 to 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

Implementation of Statement of Federal Financial Accounting Standards for Establishing Opening Balances

Effective for periods beginning after September 30, 2016, the Federal Accounting Standards Advisory Board (FASAB) released SFFAS No. 50, *Establishing Opening Balances for General Property, Plant, and Equipment*, and SFFAS No. 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials*, which allow a reporting entity, under specific conditions, to apply alternative methods in establishing opening balances. As of September 30, 2021, the DHP's implementation of SFFAS No. 50 and SFFAS No. 48 remained in process. We planned and performed our audit procedures over PP&E and I&RP opening balances accordingly.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that Management's Discussion and Analysis and other Required Supplementary 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 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 the 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. 21-04, we have also issued reports, dated November 8, 2021, 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, 2021. 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*

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Auditing Standards and OMB Bulletin No. 21-04 and should be considered in assessing the results of our audit.

Alexandria, Virginia
November 8, 2021

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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 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. 21-04, *Audit Requirements for Federal Financial Statements*, the financial statements of the Defense Health Program (DHP) as of and for the year ended September 30, 2021, 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, 2021. 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. 21-04. 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 have not been identified. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings, 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 concurred with the findings identified in our engagement. DHP's response was not subjected to the auditing procedures applied in the engagement to audit the financial statements; 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. 21-04 in considering the entity's internal control. Accordingly, this communication is not suitable for any other purpose.

Alexandria, Virginia
November 8, 2021

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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 (AF); 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
- 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-AF/Air Force Medical Service (AFMS).

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.

Exhibit 1: Material Weaknesses Identified

Accounting Area	Material Weakness
Entity-Level Controls (ELC)	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
Inventory and Related Property (I&RP)	VIII. Stockpile Materials
Accounts Payable (AP) and Related Liabilities	IX. Liabilities and Related Expenses
Budgetary Resources	X. Monitoring and Reporting of Obligations and Adjustments

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Accounting Area	Material Weakness
Information Technology (IT)	XI. 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 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 Risk Management and Internal Controls (RMIC) Program 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 System and Organization Controls [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 previously run by the Army, Navy, and AF 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 2021.

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A. Accounting and Financial Reporting Governance Structure (*Repeat Condition*)

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 RMIC Program.

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

- General PP&E
- I&RP
- AR and Associated Revenue
- AP
- Legal Liabilities
- Financial Reporting.

In FY 2020, the DHP stood up the *Military Health System Financial Policy Synchronization Working Group Charter* to develop, evaluate, adjudicate, and publish financial policies for the DHP appropriation. To help guide and prioritize DHP-wide efforts, the Financial Policy Synchronization (FPS) Working Group escalates policy requirements associated with DHP audit findings to assist with the remediation and reducing overall risk.

Cause: The DHP, in its current structure during FY 2021, does not operate as a singular entity or Enterprise organization. Rather, the DHP is the funding source for DoD's MHS. The DHP financial management organization continued to evolve during FY 2021, and as of September 30, 2021, the DHP did not 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, AF, DHA, and Health Affairs, operates independently and has 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, leading to greater ambiguity and confusion.

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Unclear delegation of authority and lack of organizational structure between the DHP and Components may result 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.

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 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*
- Accounting and reporting requirements associated with SFFAS No. 31, *Fiduciary Activities*
- 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*
- Recognition and valuation requirements set forth in SFFAS No. 44, *Accounting for Impairment of General Property, Plant and Equipment Remaining in Use*
- Accounting and reporting requirements associated with restatements per SFFAS No. 21, *Reporting Corrections of Errors and Changes in Accounting Principles*, and OMB Circular A-136, *Financial Reporting Requirements*.

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

1. Develop and distribute an Enterprise Governance Policy or consider expanding the MHS Governance Business Rules to formalize accounting and financial reporting governance for the DHP Enterprise financial reporting entity. The policy should specifically address financial and accounting governance, policies, and procedures at the Enterprise. The policy should also address an oversight role for compliance with established policies and procedures across the DHP Enterprise.

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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's Green Book and Generally Accepted Accounting Principles (GAAP).
3. Ensure the DHA Chief Financial Officer (CFO) or an equivalent position will have overall responsibility for establishing and implementing effective financial management policies, internal controls, and financial management systems for the DHP Enterprise reporting entity.

B. Entity-Level Control Design and Operation (*Repeat Condition*)

Condition: The DHP did not meet the standards for an effective internal control system, as defined in GAO's Green Book. Entity-level internal control design and operating effectiveness failures exist across all five components of internal control (i.e., Control Environment, Risk Assessment, Control Activities, Information and Communication, and Monitoring), as defined in GAO's Green Book. The DHP did not achieve any of the 17 GAO Green Book principles across the five components of internal control.

The DHP has not designed and implemented an effective process to assess and monitor the adequacy of its Components' internal control programs in support of the DHP Statement of Assurance (SoA). In FY 2021, the DHP Enterprise's SoA provided no assurance that internal control over operations, reporting, and compliance were operating effectively as of September 30, 2021 in accordance with OMB Circular A-123, GAO's Green Book, and FMFIA. In addition, the DHP Enterprise SoA for the DHP provided no assurance that the internal controls over the financial systems are in compliance with the Federal Financial Management Improvement Act of 1996 (FFMIA) as of September 30, 2021.

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 RMIC Program has not fully assessed or implemented all principles of internal controls in accordance with FMFIA and GAO's Green Book requirements in the design and implementation of ELCs, including those controls necessary in the information system environment. Components continue to operate independently; additionally, the DHP remains in the process of establishing the RMIC Program across the entity.

The DHP Enterprise has not completely documented and tested the design and operating effectiveness of its ELCs to demonstrate that the controls achieve all control objectives and are operating in an integrated manner. In addition, the Component reporting entities of the DHP have not established an effective system of internal control, as required by OMB Circular A-123.

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

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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, have 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 they are unable to sufficiently assess the risk to applicable financial reporting processes impacted by the service organization.

Recommendations: Kearney recommends that the DHP establish an Enterprise policy for the RMIC Program that requires, at a minimum, the development of ELCs at the DHP and Component levels that align with the DHP RMIC Program. The policy should require both the DHP and individual Components to perform the following:

1. Assess the DHP structure to identify all Components, MTFs, and potential changes to occur based on the ongoing reorganization. The Enterprise and individual Components should document this assessment to clearly establish the boundary and reporting structure.
2. Finalize the DHP RMIC Standard Operating Procedures. Upon finalization, the Enterprise and individual Components should distribute and implement the policy across the DHP, as identified in Recommendation #1 above.
3. Perform a data call with each of the Components and MTFs, to include any that will be onboarded in FY 2022, 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 and where the documentation is retained.
   c. Current programs, functions, and responsibilities to support the DHP's compliance with GAO's Green Book.
4. Assess the state of Component and MTFs' internal control programs and develop a formal documented strategy to incorporate the transitioning reporting entities into the DHP Enterprise RMIC Program.

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5. Maintain assessment criteria based on Government standards, best practices, and previous knowledge of DHP operations in the MHS Control Matrix.
6. Establish a mechanism to provide for adequate review of business process narratives to finalize them. In addition to helping ensure stakeholders document business processes completely and identify internal control activities accurately, the DHP RMIC team should retain any finalized documentation from Components and MTFs to support review and understanding of current processes.
7. Provide stakeholders with training to enable them to properly identify internal control activities and differentiate them from process steps and informational statements.
8. Review FY 2020 and FY 2021 results and final test plans, update control inventory through independent research, conduct understanding meetings with the DHP ELC POCs, review existing agency documentation, and crosswalk the documented controls to the respective principle in Enterprise-wide approved templates.
9. Develop and document a test plan annually for all principles and adaptable ELCs, considering changes in the entity's ELC inventory, the results of the previous assessment, and applicable recommendations provided by internal control oversight bodies and/or external auditors.
10. Document and implement policies and procedures for the monitoring of third-party service organization controls in accordance with GAO's 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*.
11. 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.
12. 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.
13. 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 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

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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 2021, 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 five DHP Components included in Advana utilize eight 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) 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 2020 Quarter (Q) 4 through FY 2021 Q4 to coincide with the delivery of final financial statements. Delivery of completed reconciliations ranged from seven weeks after quarter-close to 15 weeks after quarter-close.

The DHP's Standard Accounting and Reporting System (STARS) – Field Level (FL) GL system is not in substantial compliance with the FFMIA. 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 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 remains in the process of refining its understanding of UoT data produced from Advana or GL system data, impacting the DHP's ability to timely support critical audit requests during the FY 2021 financial statement audit. Specifically:

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- Complete and accurate submissions were not provided timely. Although partial delivery for each request was on time, final and complete submissions were more than 30 days overdue for five out of eight data sets requested
- Interim expense populations provided by the DHP did not include proper exclusions, resulting in large offsetting balances remaining in the testing data
- The DHP was not able to provide interim consumables populations for Undelivered Orders (UDO) balances, as applicable to SMA-AF.

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.

The DHP's use of eight 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 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 DHP remains in the process of refining its understanding of its Advana data. Additionally, the reorganization of the DHP has impacted management's understanding of the associated financial data, which now includes inputs from multiple, complex GL systems. Further, Advana is not currently part of the DHP internal control environments over financial reporting. The DHP does not rely on or use Advana for any financial reporting validation procedures or managerial reporting requirements.

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 cannot consistently generate timely and accurate GL populations across its multitude of systems and continues efforts to establish criteria to isolate and exclude transactions arising from non-economic events (e.g., cost transfers). Additionally, the DHP is not able to provide transaction-level consumables detail, impacting the ability to determine the accuracy of multiple financial statement line items. Overall, the lack of timely and fully refined population parameters inhibits the DHP's ability to strengthen monitoring activities over financial reporting.

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

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. Continue efforts to modify the Memorandum of Understanding (MOU) with its service organization, as necessary, to establish timely formal delivery of data and applicable reconciliation packages to the DHP within a timeframe that allows the DHP to complete the quarterly reconciliation effort prior to issuance of final financial statements.
3. Utilize the Advana SOC 1® report (when issued) to place reliance on service organization controls in order to expedite validation of data and reconciliation packages.
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 performing 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.
6. Coordinate with the service organization Advana team to continue efforts to resolve variances under research. The DHP should determine the financial statement impact of the unexplained variances identified.
7. 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.
8. 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.
9. Review and update all population parameters between Component entities for common systems to ensure the consistency and completeness of sample populations.
10. Update population parameters using a rules-based approach, leveraging field and character identifiers that can be applied across a transaction universe.
11. Review and update the waterfall sequence of population assessable unit parameters to ensure consistency with documentation provided to external stakeholders.
12. Implement system and process changes to interface consumables activity in General Accounting and Finance System – Reengineered (GAFS-R) at the transaction level.
13. 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.

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

Background: The DHP's service organization for financial reporting posts monthly journal voucher (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 posts various adjustments to the 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.

Included in the monthly and quarterly financial reporting processes are the postings 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 eliminations, which are those outside of the DHP. Prior to execution of the elimination entries, trading partner seller-side adjustments, recorded as a JV or a trading partner report entry, align balances between trading partners to resolve the intragovernmental account balance discrepancies. The *Financial Management Requirements for Trading Partner Eliminations Memorandum* (FPM-19-03) requires DoD reporting entities that are unable to track trading partner data at the transaction level to adjust their balance to the supportable data reported by the trading partner.

Condition: The DHP's financial statements contain material unsupported JV adjustments. During FY 2021, unsupported adjustments, as self-classified by the DHP's service organization, were posted on behalf of the DHP Components in Q1 through Q2. Of approximately 1,650 JVs and TBIAs recorded, 49 were classified as unsupported.

The DHP Components could not sufficiently support the review and approval of DDRS-B and DDRS-AFS JVs manually recorded by the DHP service organization. Nine of 57 JVs selected for testing were noted as exceptions.

The DHP, in coordination with its service organization, has not ensured adjustments processed and recorded during the quarterly financial statement compilation process are fully supported by underlying transaction-level data, and as of Q3 FY 2021, it has not fully completed reconciliations from underlying source data to the DDRS-B TB adjustments.

Trading partner seller-side adjustment JVs and trading partner report entries, recorded 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 the adjustments.

Cause: The DHP financial reporting environment is complex, necessitating a high 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.

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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. Many of the information systems in use were not designed for recording and reporting activity for the purpose of preparing financial statements in accordance with GAAP.

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 has not established policies or procedures requiring Components 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 Enterprise-level financial statements.

Effect: As a result of the magnitude of unsupported JVs and other adjustments recorded during financial statement preparation, the DHP cannot attest to the accuracy, validity, and completeness of its FY 2021 opening balances and the financial statement balances impacted by such adjustments recorded during FY 2021. In the Q3 FY 2021 Unsupported JV Financial Statement Impact Analysis, the DHP identified $19.2 billion of unsupported adjustments in the Balance Sheet, ($19.2) billion to the Statement of Net Cost, $5.9 million to the Statement of Change in Net Position, and no impact to the Statement of Budgetary Resources.

Misstatements to the DHP Enterprise financial statements may not be detected and corrected timely, and the DHP is unable to reconcile from its detailed feeder file transactions to its financial statements.

The volume and dollar amount of unsupported JVs and adjustments 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, perform the following:

1. Continue to perform quarterly analyses of the unsupported DDRS-B JVs, DDRS-AFS JVs, and TBIAs 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 adjustments. Upon completion of each analysis, a remediation plan should be evaluated and updated by JV category to set a path forward to resolve the JV requirement. This analysis should include review of the assigned "supported" or "unsupported" classification of each JV category to ensure the JV log accurately reflects the correct classification.

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2. Continue efforts to reduce the number and dollar amount of JVs recorded in DDRS by coordinating with 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.
3. Update or implement appropriate policies, procedures, and MOUs to facilitate coordination and communication between the DHP Components and all of its service organizations 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. MOUs should establish thresholds appropriate for the DHP to ensure adjustments material to each relevant DHP Component are reviewed and approved prior to being recorded in DDRS.
4. Continue to refine the oversight of DHP Components to ensure review of each JV adjustment is timely documented on the JV Review Checklist and timely concurrence is provided to the respective service organization site. The DHP should use information gathered from oversight to inform further corrective actions needed to ensure preparation errors are detected and corrected timely.
5. Continue to perform periodic analyses to determine the financial statement line item impact of unsupported and unreconciled DDRS-B adjustment balances. This analysis should incorporate efforts to define relationships between the DDRS-B adjustment files to identify the net impact to the financial statements.
6. Continue to work to obtain detailed transaction-level data for all DDRS-B adjustments and feeder files, as necessary.
7. 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.
8. Continue to perform an analysis of the unsupported adjustments and develop a strategy to validate the inclusion of the unsupported balances on the DHP TB.
9. As appropriate, continue efforts to reverse historical, unreconciled DDRS-B adjustments and to obtain sufficient documentation to support the reversal of the balances and document the net impact to the financial statements.
10. Implement policies and procedures to ensure that the trading partner coordination and reconciliation process, as well as the process to review and approve adjustments and eliminations, is consistently applied across the DHP Components.
11. Continue efforts to formalize policies and procedures to perform reconciliations for both buyer- and seller-side trading partner activity at the transaction level on a monthly basis and coordinate directly with trading partners to resolve differences.
12. Continue efforts to formalize policies and procedures requiring the DHP to coordinate with trading partners and its service organization to review and 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.
13. Work with the General Fund Enterprise Business System (GFEBS) Program Management Office (PMO) to incorporate the trading partner code and correct the Federal/non-Federal flag at the GFEBS transaction level.

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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 comprises 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, the 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.

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

- The DHP's financial statements include an unsupported/unreconciled opening FBWT balance of $194 million
- 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 year-end actual or estimated suspense and SOD balances
- The DHP, in coordination with its service organization, does not have an effective reconciliation process to fully support undistributed adjustments recorded during the financial statement compilation process performed by its service organization.

Cause: The DHP's Balance Sheet includes FBWT activity excluded from Department 97 Reconciliation Tool (DRRT) and Consolidated Cash Accountability System (CCAS) reconciliation tools, resulting in unreconciled/unsupported FBWT balances.

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SOD and Suspense UoTs are not available after quarter-end in a timely manner to perform sufficient analysis for financial reporting and often do not identify the responsible entity for each transaction. The DHP and its service organization have not designed and implemented a methodology to determine the financial reporting impact of the SOD and suspense balances to the DHP's financial statements.

FBWT reporting and reconciliation controls performed on behalf of the DHP are ineffective due to incomplete policies and procedures, and failure to adhere to defined policies.

Effect: Without an effective reconciliation process, the DHP may be unable to assess the potential risks to the accuracy and completeness of FBWT or determine the total unsupported differences between its recorded FBWT and the balance reported in CARS. In addition, DHP management may also be unaware of the potential risk of a financial statement misstatement.

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

1. Identify impediments to the TI-97 FBWT reconciliation process (e.g., excluded activity from the DRRT, CCAS, TI-97 budget clearing accounts, and SODs) and develop compensating controls or develop new systems to reconcile any excluded FBWT activity or, through documented materiality analysis, indicate that management accepts the risk of potential misstatement.
2. Perform root cause analysis to assess underlying business processes which are triggering the high volume and dollar amount of undistributed transactions.
3. Develop, implement, and document an effective reconciliation process for identifying any unmatched disbursements and collections and ensure that all resulting adjustments are fully supported.
4. Develop and implement a methodology to identify the actual or estimated impact of SODs and suspense accounts for recording and reporting into the GLs and financial statements.
5. 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 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

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to TRICARE beneficiaries who are either covered by other insurance or who receive care which is uncovered. The DHP Components utilize a billing and collection system as a subsidiary ledger to track and process collections on medical billings.

MTFs also provide medical services for beneficiaries who 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.

The provision of care by MTFs sometimes results in revenue earned from the public. Third-Party Collections (TPC) relate to medical services provided to TRICARE beneficiaries with other health insurance (e.g., from their employers). Medical Service Accounts (MSA) include medical services provided and charged directly to eligible beneficiaries (e.g., elective services). Medical Affirmative Claims (MAC) relate to medical services provided when another party is liable (e.g., homeowners or automobile liability insurer).

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 are provided at MTFs daily, and per DHA-Interim Procedures Memorandum (IPM) 18-016, these services are required to be coded within three business days for outpatient (OP) encounters, 15 days for ambulatory procedure visits (APV), and 30 days for inpatient (IP) encounters from the time the patient is discharged, which initiates the billing process. Medical coding consists of taking the medical services rendered to a patient and entering the applicable codes using the DHA-distributed coding tables. DHA contracts with a third party to perform annual audits over the 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 2019 coding audit, which represents an audit of medical records that were coded in FY 2018. During the audit, approximately 2,500 coded encounters were selected for testing, consisting of both billable and non-billable claims, across all MTFs.

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A. Accounting and Reporting of Medical Services Provided (*Repeat Condition*)

Condition: The DHP 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.

- Medical services provided by DHA AF-related MTFs to Federal beneficiaries are accounted for on a cash basis of accounting, which does not comply with GAAP. The MTFs issue bills for medical services but records associated Federal revenue upon cash receipt in their GL system. DHA does not have processes in place to correct the cash basis of accounting for financial reporting purposes
- AR associated with medical services provided to Federal trading partner beneficiaries may not be processed and/or 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
- DHA and its MTFs do not consistently and accurately present Revenue and AR at net realizable value (NRV). The DHP has not established a comprehensive allowance for uncollectible accounts or alternatively adjusted Revenue and AR to reflect NRV, as appropriate
- The DHP does not have a process in place to reconcile public Collections in Transit, Collections, and Revenue activity between ABACUS and the respective GL systems. The DHP also does not have a process in place to reconcile Federal AR, Collections, and Revenue activity between ABACUS and its various GL systems.

DHA and MTFs receive quarterly prospective payments in advance of care provided from the Medicare-Eligible Retiree Health Care Fund (MERHCF). DHA and MTFs do not have formalized processes in place to track health care encounters for MERHCF beneficiaries for accounting purposes, resulting in no transactional patient-level data to support the direct care revenue recognized by the DHP. The DHP, however, recognizes the revenue upon the transfer of funds, which is not in compliance with Federal accounting standards. There is also insufficient evidence that appropriate and consistent cut-off accounting activity occurs at the MTF level associated with care provided to MERHCF beneficiaries. The DHP has not yet implemented appropriate and sufficient levels of management control and reconciliation processes to ensure the adequacy and completeness of the data required for its financial reporting processes associated with direct care.

The DHP does not have a documented internal control activity for conducting an eligibility check within DEERS, verifying the most recent information is being used to determine a patient's PATCAT.

The DHP did not provide or maintain sufficient audit evidence to support the validity of AR balances within the billing and collection subsidiary ledger. DHP remediation efforts remained in process to correct AR transactions noted as invalid because they were previously collected and

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never closed in the system and to provide sufficient documentation to support amounts billed for services provided.

Cause: The DHP has not formulated or implemented complete Enterprise-wide accounting policies or guidance for its MTFs to ensure consistent and accurate accounting of medical services provided in accordance with GAAP. Additionally, formalized accounting policy and procedures have not been developed to appropriately account for AR and associated Revenue at NRV.

The DHP has not established effective business processes with associated internal controls to properly recognize Federal medical service revenue and associated AR for DHA AF-related MTFs using the accrual basis of accounting. Specific to the MERHCF, the DHP has 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 with associated internal controls to properly recognize medical service revenue and associated AR from the public, using the accrual basis of accounting.

The DHP Enterprise has not effectively implemented policy and guidance at the MTF level for patient check-in or ancillary procedures regarding eligibility verification for medical services provided. The DHP does not have a consistent process to document and demonstrate the verification of patient eligibility prior to providing medical services. Moreover, CHCS does not keep record of when the most recent eligibility check was performed and which PATCAT determination was made at the time of the query.

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 Statement of Budgetary Reporting (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 DHP MTFs, 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 Component reporting entities. In addition, the DHP should 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 in accordance with applicable Federal Accounting Standards. 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 MTF. 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. The methodology should adjust gross AR and associated revenue to reflect NRV.
6. 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.
7. Perform documented reconciliation of medical AR recorded in the subsidiary ledger with medical AR recorded for financial reporting, including supervisory review and approval.
8. 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.
9. Review supporting documentation and retention requirements over valuation of patient billings to ensure the DHP's ability to successfully respond to external audit requests.

B. Medical Coding Accuracy (Repeat Condition)

Condition: The DHP has not implemented effective medical coding procedures to ensure the accuracy of medical coding applied over IP, OP, APVs, and inpatient professional services round (IPSR) health care encounters. The most recent third-party medical coding audit report released during FY 2020, entitled *Fiscal Year 2019 Military Treatment Facility External Coding Audit Findings and Recommendations*, identified the rate of coding accuracy significantly below the required 97% threshold prescribed within DoDI 6040.42:

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Exhibit 2: Pass Rates Comparison for Billable vs. Non-Billable Records

Record Type	Pass Rates	
	Billable	Non-Billable
IP	76.74%	79.18%
OP	43.18%	40.65%
APV	45.83%	68.34%
IPSR	57.14%	57.46%

The DHP's remediation activities to sufficiently address the coding inaccuracies remained in process during FY 2021.

Cause: The findings and recommendations included in the FY 2019 medical coding audit indicate that the DHP does not have sufficient clinical supporting documentation that clearly and specifically address the procedures performed during patient encounters for accurate medical coding.

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.

Recommendations: Kearney recommends that the DHP perform the following:

1. Continue to 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 appropriate stakeholders across DHA.
2. Utilizing the coding accuracy results for billable encounters, assess the financial reporting impact of coding inaccuracies found during the third-party audits. Appropriate analysis of the error rates should be conducted to determine the impact of error rates over applicable financial statement line items (e.g., Revenue and AR).

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. The DHP has not fully designed and implemented consistent policies, procedures, or controls to effectively record and report capitalized GE across the DHP Components in

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accordance with GAAP, as promulgated by FASAB. The procedural instruction for GE, provided in draft form in March 2019, remained in draft form as of September 30, 2021.

Complete inventory of the DHP capitalized GE was not completed in FY 2021. Of the inventories completed across the DHP Components, results were not generated timely and counts were not executed consistently across the DHP Components. The inventory control procedures executed in FY 2021 were not completed in compliance with DoDI 5000.64, *Accountability and Management of DOD Equipment and Other Accountable Property*.

The DHP did not demonstrate sufficient existence and completeness for GE which was recorded for FY 2021. The results of GE existence testing procedures identified assets for which the DHP was unable to support observation procedures. DHP could not locate assets or alternative procedures, such as follow-up requests for additional documentation, were not sufficient to support asset existence. The results of GE completeness testing procedures identified assets on-site at the MTFs that could not be traced to the APSR, and the DHP was unable to provide sufficient evidence to account for medical equipment acquisition cost. The DHP could not locate or did not provide sufficient audit evidence to support the existence of 7% of 146 tested assets. The DHP did not record or did not provide sufficient appropriate evidence to support approximately 25% of 163 tested assets, which were selected while performing testwork at DHP locations and through virtual procedures (i.e., completeness of DHP recorded assets).

Cause: The DHP RMIC Program activities performed in support of the DHP annual SoA do not currently incorporate GE as an assessable unit. Risk assessment procedures have not been conducted to identify financial reporting risks associated with GE and the extent of internal controls in place to address identified risks, as well as to identify internal control gaps which may exist.

The reorganization of the DHP has added complexity to operations, requiring a redesign of the control environment as operations and processes are consolidated from the SMA under DHA. Further complexity is attributable to the transition of GE oversight and reporting responsibilities from the DHP Components to the DHA Medical Logistics (MEDLOG) Division. Under the reorganization plans, DHA MEDLOG will be taking full ownership of all DHP Component GE as of October 01, 2021.

DHP management has not designed and implemented policies, procedures, and controls consistently across the DHP to ensure that GE is appropriately and accurately reported in the financial statements. As part of remediation efforts conducted in response to the prior-year NFR, the DHP has formulated a draft procedural instruction for GE. The GE guidance was drafted as of March 2019 but has not been finalized as of September 30, 2021.

Effect: Without effectively designed and consistently implemented internal controls for the management and reporting of GE across the organization, the DHP cannot assert 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 16% of tested assets, which may represent potential misstatements to the PP&E balance as of September 30, 2021.

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Recommendations: Kearney recommends that the DHP perform the following:

1. Establish an Enterprise-wide accounting policy for GE that requires annual inventories, tracking GE, and proper cost classification in accordance with SFFAS No. 6, to include appropriate footnote disclosures.
2. Update existing procedures to ensure that consistent and compliant wall-to-wall inventory procedures are performed across the DHP in a timely manner and in accordance with DoDI 5000.64, *Accountability and Management of DOD Equipment and Other Accountable Property*.
3. Develop and communicate internal deadlines for annual inventory certification submission within the DHP Components before submission to the DHP Enterprise.
4. As part of the DHP RMIC Program activities performed in support of the DHP annual SoA, ensure GE is incorporated as an assessable unit. Risk assessment procedures should be conducted to identify financial reporting risks associated with GE and the extent of internal controls in place to address identified risks, as well as to identify internal control gaps which may exist.
5. Complete ongoing efforts to verify the existence and completeness of GE for the purpose of bringing the GE portfolio to record for financial reporting.
6. 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.
7. 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.
8. 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 (IUSD); heritage assets; leases; and leasehold improvements. The DHP reported PP&E, net of accumulated depreciation and accumulated amortization, to be $3.8 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.

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Condition: The DHP PP&E valuation as of September 30, 2021 is not in accordance with GAAP. The PP&E balances have not been sufficiently valued at historical cost in accordance with valuation techniques promulgated by SFFAS No. 6 or SFFAS No. 10, as appropriate. 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.

- The DHP has not completed an assessment of IUS or IUSD in order to properly identify and account for IUS for financial reporting purposes. The opening balance of DHA's IUSD, recorded at $1.0 billion as of October 01, 2020, consisted entirely of the MHS GENESIS. MHS GENESIS is not valued in accordance with historical cost requirements prescribed within SFFAS No. 10. Outside of valuing MHS GENESIS, the DHP has not begun valuation efforts over remaining IUS or IUSD using alternative valuation techniques in accordance with SFFAS No. 50
- The DHP does not have a process in place to record real property CIP related to Operations and Maintenance (O&M)-funded projects for financial reporting. The DHP does 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
- DHA, in coordination with Naval Facilities Engineering Systems Command (NAVFAC), does not have a complete process in place to track real property CIP expenditures reported in NAVFAC's financial system, nor reconcile the capitalized expenditures to individual real property CIP projects. No alternative procedures have been developed to capture real property CIP expenditures related to DHA projects for financial reporting purposes
- DHP Component reporting entities do not have sufficient supporting documentation (e.g., invoices and receipt and acceptance documentation) to support the historical cost requirements of SFFAS No. 6 for reported GE.

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 or SFFAS No. 10. 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 during FY 2021.

As part of remediation efforts conducted in response to the prior-year NFR, the DHP has formulated draft accounting guidance for GE and real property CIP asset classes. The draft guidance has not been finalized as of September 30, 2020, nor does it specifically address valuation for opening balances under SFFAS No. 50. On September 7, 2021, DHA published Administrative Instruction 7040.01, *Defense Health Program Internal Use Software*. The instruction has been published, but no formal training or changes have been implemented in FY 2021.

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DHA has not applied its capitalization policies to real property CIP projects funded by O&M appropriations. Additionally, DHA has not established effective internal controls to track and record capitalized costs related to O&M-funded CIP.

DHA, in coordination with NAVFAC, has not developed sufficient procedures over the NAVFAC-executed Military Construction (MILCON) expenditures to ensure real property CIP balances reported within the DHA financial statements are complete and accurate. DHA, in coordination with NAVFAC, was not sufficiently prepared for a NAVFAC system migration that occurred in FY 2021 to appropriately identify and account for real property CIP projects owned by DHA.

Effect: The DHP is unable to accurately and appropriately value its PP&E assets for FY 2021 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 2021 PP&E opening balances at historical cost in accordance with SFFAS No. 50.

The DHP's PP&E as of September 30, 2021 does not reflect historical cost as required by SFFAS No. 6 or SFFAS No. 10, and the DHP's opening balances for FY 2021 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 $3.8 billion may be materially misstated as presented within the DHP's 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 Statement of Net Cost and Balance Sheet, respectively. Additionally, the DHP is unable to accurately account for the existence, completeness, or valuation of real property CIP managed by NAVFAC in accordance with Federal accounting standards. Accordingly, the DHP's recorded balance for PP&E is potentially understated by the NAVFAC-executed MILCON expenditures as of September 30, 2021.

Recommendations: Kearney recommends that the DHP perform the following:

1. Develop an Enterprise-wide accounting policy for PP&E, which specifically addresses historical cost valuation in accordance with SFFAS No. 6, SFFAS No. 10, 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 and SFFAS No. 10.
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 required to perform.

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6. Detail requirements for valuation of new acquisitions that are compliant with SFFAS No. 6.
7. Coordinate with constructions agents, 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.
8. Provide training to DHP personnel to ensure policies and procedures to track and record O&M-funded CIP are implemented accordingly.
9. 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.
10. Develop a project-level crosswalk between systems to identify the DHA real property CIP projects and the related expenditures. The DHP should formalize a monthly reconciliation process that includes the DHA MILCON funding and expenditures executed by the DoD construction agents. The reconciliation procedure should require timely reporting of results, as well as review and approval signoffs from DHA and DoD construction agent personnel. The DHP should also perform appropriate actions based on the reconciliation results.
11. As appropriate for future or ongoing system migrations or system changes, conduct a complete assessment over the impact to financial reporting requirements to ensure appropriate changes can be included within the system change or compensating internal control activities can be developed for implementation in the new environment.

VIII. Stockpile Materials (*Repeat Condition*)

Background: DHP Components are required to maintain various medications for the DoD to respond to a pandemic or other public health emergency. DHA maintains Service-Level Agreements (SLA) with Federal entities to purchase medications on behalf of DHA. DHA also maintains SLAs to purchase medications and to store and distribute medication materials for medical preparedness. Medications and materials purchased for DHA by other Federal entities remain at the manufacturing facility until such time that they need to be administered.

Condition: The DHP did not account for Stockpile Materials in accordance with requirements set forth in SFFAS No. 3. As a result of the ongoing assessments to identify programs which maintain Stockpile Materials, the DHP has not fully transitioned to the consumption method of accounting as required for Stockpile Materials under SFFAS No. 3. The purchases method of accounting is still in use for any programs containing Stockpile Materials which have yet to be identified. The purchases method of accounting is not allowable under SFFAS No. 3 for Stockpile Materials.

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During FY 2021, the DHP prioritized its Pandemic Influenza Program to identify and record Stockpile Materials, while continuing efforts to obtain Stockpile Materials data from MTF locations for the purpose of financial reporting requirements. The DHP Components' remediation efforts to validate the recorded quantities and amounts of Stockpile Materials remain in process.

The DHP was unable to provide a Stockpile Materials population that fully reconciled to its financial statements as of June 30, 2021. A variance of $8 million was noted between the Stockpile Materials population provided and the financial statements as of June 30, 2021.

Cause: The DHP has not designed or implemented policies, procedures, and controls to ensure that Stockpile Materials are completely, appropriately, and accurately captured in the financial statements in accordance with GAAP. 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. DHA and the SMAs have not incorporated Stockpile Materials into their RMIC Program as part of management's responsibility for evaluating its system of internal control.

Additionally, the DHP does not have a consolidated system, document, or file utilized to maintain Stockpile Materials. The Stockpile Materials population is manually created, and changes in Stockpile Materials balances each quarter are manually calculated. On-hand quantities and purchase prices are sourced from various systems, documents, and data sources, and they must be aggregated together to determine the quarterly balance.

Effect: The DHP is unable to accurately account for the existence, completeness, or valuation of Stockpile Materials in accordance with Federal accounting standards. Accordingly, the DHP's balance of I&RP for FY 2021 is understated and period expenses are misstated as they reflect current-year purchases instead of usage (consumption).

Due to the lack of controls surrounding Stockpile acquisitions and tracking, the DHP was unable to sufficiently support the value of Stockpile Materials recorded or determine the value of any misstatement. Additional assessments are required to determine if additional programs meet the Stockpile Materials reporting requirements and additional levels of the Pandemic Influenza Program need to be assessed, validated, and further reported. Period expenses are overstated by any Stockpile Materials acquisitions occurring in FY 2021.

Recommendations: Kearney recommends that the DHP perform the following:

1. Develop and implement a strategy to verify the existence and completeness of Stockpile Materials held by DHA and the SMAs or held by third-party custodians on behalf of the DHP.
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. Incorporate Stockpile Materials as an assessable unit within the DHP RMIC Program.

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4. Implement policies, procedures, and controls for the end-to-end business process of Stockpile Materials. The policy, procedures, and controls should formally cover acquisition, receipt, issuance, transfers, inventory management, and disposal activities.
5. Establish appropriate SLAs with applicable service organizations identified within the Stockpile Materials end-to-end lifecycle.
6. Complete ongoing efforts to verify the existence and completeness of DHP-owned Stockpile Materials for the purpose of bringing the portfolio to record for financial reporting.
7. Complete ongoing efforts to value Stockpile Materials in accordance with Federal accounting standards. The DHP should consider the valuation techniques within SFFAS No. 48 in establishing its opening balance of Stockpile Materials.
8. Establish appropriate accounting policy to value new acquisitions and the consumption of existing Stockpile Materials in accordance with SFFAS No. 3. New acquisitions should be recorded using the consumption method of accounting defined in SFFAS No. 3.

IX. 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, 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 waste; 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.
Condition: The DHP does not sufficiently account for its liabilities and related expenses. Specifically, the DHP and its Components do not have a complete or comprehensive process to record estimated AP and expenses for goods and services received but not yet billed in accordance with SFFAS No. 5.

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, nor a process to validate intragovernmental payment activity when receipt and acceptance cannot be performed prior to payment.

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:

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

The DHP is unable to sufficiently support the substantive validity, accuracy, and completeness of non-payroll expenses. Testing identified exceptions in 137 of 201 non-payroll expense sampled transactions, compromising 38% of the balance tested. The most common findings are presented below:

- One hundred and four samples resulted in exceptions where the DHP did not provide and/or maintain sufficient documentation to support the sampled transactions recorded
- Five NPE samples resulted in a substantive exception where the sampled expense was recorded in the incorrect period. The documentation received indicated that the sample expenses were incurred in FY 2020 but not recorded until FY 2021
- Twenty-one samples resulted in a classification exception where the sampled expense was incorrectly classified as either a Federal or Non-Federal transaction

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 across all relevant business processes. DHP Components remain in the process of developing a comprehensive AP accrual methodology which takes into consideration all business processes, as determined necessary for financial reporting. Additionally, DHP Components do not have a process in place to validate post-payment activity when receipt and acceptance cannot be performed.

For E&DL and settlements and judgments, DHP Components lack comprehensive policies and procedures to monitor and 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.

The DHP does not consistently obtain and/or maintain sufficient supporting documentation to validate if goods and services are received prior to accepting the invoice. While the DHP has established processes that align with contractual requirements for payment processing, those processes have not been designed to sufficiently achieve financial reporting objectives.

The DHP has also not implemented sufficient internal control activities to properly classify expenditures as Federal and Non-Federal. While system limitations have inhibited proper trading partner identification, no compensating internal controls or processes were identified.

Effect: The lack of comprehensive Enterprise-wide policies and guidance has resulted in inconsistent accounting treatment across the DHP, 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.

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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 perform the following:

1. Continue the 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. Expand the current AP accrual methodology to include all GL systems and all financial reporting limits, as determined appropriate.
3. 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.
4. Continue to 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.
5. 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.
6. Collaborate with the Office of General Counsel (OGC) to determine and document the legislative basis by which the Military Departments pay for E&DL and settlements and judgments, on behalf of SMA Components, as applicable; and evaluate whether amounts are being charged to the correct appropriation.
7. Implement a process for performing quarterly data calls to the DHP Enterprise to generate a complete and accurate listing of potential environmental liabilities.
8. Coordinate with the Office of the Under Secretary of Defense for Acquisition and Sustainment to obtain the Defense Environmental Programs report to Congress each year. An assessment should be made to understand whether any programs covered in the report are applicable to the DHP Enterprise operations and, therefore, may require financial reporting or disclosure of associated environmental liabilities.
9. Evaluate the current control environment and design/establish control activities to verify receipt and acceptance of services prior to entitlement and disbursement or through timely post-payment reviews. These control activities should be designed in a manner that allows management to have reasonable assurance that the risk of material misstatement will be reduced to a sufficiently low level.
10. Improve record retention over receipt of goods and services and supporting documentation over non-payroll expense transactions. Sufficient supporting documentation requirements should be implemented to demonstrate proper receipt and acceptance has occurred for payment processing (e.g., timesheets, packing slips, contract performance statements, proof of enrollment).
11. Assess current business operations to implement compensating control activities to address proper cost classification between Federal and Non-Federal transactions. The

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DHP should coordinate any newly designed controls activities with remediation efforts planned to address system limitations for cost classification.

12. Assess existing payment procedures, in conjunction with planned remediation for establishing appropriate AP accruals, and determine if additional internal controls are required to mitigate financial reporting risk associated with recording transactions in the incorrect period.

X. Monitoring and Reporting of Obligations and Adjustments (*Repeat 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 UDOs; Delivered Orders, Unpaid (DOU); UDO-Paid (UDOP); and Unfilled Customer Orders (UFCO) on a quarterly basis as part of Dormant Account Review – Quarterly (DAR-Q). The DAR-Q process is required by the DoD Financial Management Regulation (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 DAR-Q 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.

Federal reporting entities recognize and report downward adjustments during the current FY to obligations that were originally recorded in a prior FY. Downward adjustments are required to be classified utilizing specific USSGL accounts in accordance with the TFM. The DHP is responsible for developing policies and procedures to ensure downward adjustments are appropriately supported, comply with all relevant regulations, and are properly reviewed and approved.

Condition: The DHP's DAR-Q process is not operating effectively across all Component entities to review, assess, and close stale obligations on a timely basis and has not been effectively implemented to verify completeness of the populations used as part of the DAR-Q.

The DHP is unable to sufficiently support the substantive accuracy of downward adjustments recorded in USSGL No. 4871, *Downward Adjustments of Prior-Year Unpaid Undelivered Orders – Obligations, Recoveries*. Testing identified exceptions in 145 of 250 sampled transactions, comprising 67% of the balance tested. The most common findings are presented below:

- Seventy-four exceptions were noted because the DHP did not prepare and/or maintain sufficient documentation to support the transactions recorded
- Thirty-five exceptions were noted as a result of the DHP processing corrections of administrative errors that should not have impacted the financial statements but improperly generated accounting entries in the GL systems

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- Twenty-two exceptions were noted as a result of robotic process automation deployed by the Navy BUMED, which prompted systemic de-obligations without supporting documentation or review and approval. Three out of 22 sampled actions were subsequently reversed, indicating that the de-obligations were invalid.

Cause: The DHP's DAR-Q has not been effectively designed or implemented across all Components. In addition, the DAR-Q has not been designed to fully capture the DHP's open obligation activity, as certain obligation classes have not been incorporated. Further, the DAR-Q does not currently include all obligations within each DHP financial reporting entity.

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.

The DHP's decentralized control environment lacks clear policy and procedures for standard treatment of de-obligations and adjustments to prior-year obligations. Additionally, the DHP has not developed a process to evaluate entries to USSGL No. 4871 that are automatically generated in the GL system but require reversal for administrative changes. Finally, the DHP has deployed robotic process automation that results in unprompted and unsupported GL entries.

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 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 Treasury timely.

The DHP cannot attest to the accuracy and completeness of transactions recorded in USSGL No. 4871. Line 1071, *Unobligated balance from prior year budget authority, net*, may be misstated on the DHP SBR. Line 1021, *Recoveries of prior-year unpaid obligations*, may be misstated on Standard Form (SF)-133, *Report on Budget Execution and Budgetary Resources*.

Recommendations: Kearney recommends that the DHP perform the following:

1. Establish formalized policy and procedures for the DAR-Q process as prescribed by OUSD(C). The formal policy should prescribe timeframes for de-obligation actions after identification and how to handle contracts still in the contract close-out process.

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2. In coordination with OUSD, develop formalized supporting documentation to demonstrate that the DAR-Q population ties and agrees to the TB, prior to isolating obligation activity for specific monitoring.
3. 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-obligation initiative and establish cut-off dates for mandatory de-obligation; and process the de-obligation actions to remove invalid obligations.
4. Evaluate processes currently in place to adjust obligations in each DHP GL system and at each Component to identify procedural and documentation gaps. This analysis should include administrative adjustments, financial adjustments, and de-obligations.
5. Develop standardized policies and/or guidelines that ensure proper documentation is prepared, reviewed, approved, and retained in accordance with 31 United States Code (U.S.C.) Section 1501, *Documentary evidence requirement for Government obligations*. This should include internal controls that ensure transactions are accurate and properly supported.
6. Design and implement a recurring analysis to identify and reverse improper entries to USSGL No. 4871 resulting from administrative changes to previously recorded obligations. The DHP should consider whether this process would benefit from the design and release of a standard data call to identify activity to be reversed.
7. Modify robotic process automation to serve as the identification point for potentially stale obligations. De-obligation should not occur until the vendor confirms that all invoicing has occurred and that contract close-out is appropriate.
8. Perform internal control testwork under the RMIC Program to determine if the newly implemented policies and procedures have been implemented effectively.

XI. 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 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 27 financially significant systems, including five GL and financial reporting systems, five health IT systems, and 17 other key feeder systems and environments. The following is a summary of critical deficiencies:

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- 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
- 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 items noted in the prior years by developing and disseminating Enterprise-wide policies, procedures, and other guidance, the communication, implementation, training, monitoring, and enforcement of those policies and procedures at the user community level is still in progress, and remediation efforts are evolving as the DHA organization structure changes. The DHP prioritized remediation of many prior NFRs through four Enterprise-wide CAPs completed in FY 2021, but it did not fully resolve the underlying conditions. The deficiencies noted above result from a multitude of causal factors, with the most pervasive ones being the lack of complete and consistent implementation and enforcement of IT policies and procedures; inconsistent or inadequate control implementation and/or performance; and focused remediation efforts that resulted in weaknesses in other areas continuing. Specifically, the conditions noted above occurred primarily due to a combination of the following reasons:

- Control Implementation and Operation
  - Controls were not implemented during FY 2021
  - Controls were implemented but not operating effectively during FY 2021
- 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 areas
- CAP Implementation
  - Remediation efforts are ongoing and evolving as the organization structure changes
  - CAPs associated with FY 2018, FY 2019, or FY 2020 IT NFRs were not completed or not prioritized during FY 2021.

Effect: Without complete and consistent implementation, monitoring, and enforcement of policies and procedures, 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.

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Recommendations: Kearney recommends that the DHP perform the following:

1. Provide guidance and oversight to the DHP Components, MTFs, and service organizations on the assignment of responsibilities for the consistent implementation of internal controls to strengthen overall IT governance.
2. Continue communication and reinforce 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.

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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) 2020 financial statements, we noted several issues that were related to internal control over financial reporting. The status of the FY 2020 internal control findings is summarized in ***Exhibit 3***.

Exhibit 3: Status of Prior-Year Findings

Control Deficiency	FY 2020 Status	FY 2021 Status
I. Accounting and Financial Reporting Governance and Entity-Level Control Design and Operation	Material Weakness	Material Weakness
II. Financial Reporting – Universe of Transaction Reconciliations	Material Weakness	Material Weakness
III. Financial Reporting – Defense Departmental Reporting System Adjustments	Material Weakness	Material Weakness
IV. Fund Balance with Treasury	Material Weakness	Material Weakness
V. Medical Revenue and Associated Receivables	Material Weakness	Material Weakness
VI. General Equipment Existence and Completeness **VII. Valuation of Property, Plant, and Equipment**	Material Weakness	Material Weakness
VIII. Stockpile Materials	Material Weakness	Material Weakness
IX. Liabilities and Related Expenses	Material Weakness	Material Weakness
X. Monitoring and Reporting of Obligations and Adjustments	Material Weakness	Material Weakness
XI. 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 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. 21-04, *Audit Requirements for Federal Financial Statements*, the financial statements of the Defense Health Program (DHP) as of and for the year ended September 30, 2021, 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, 2021. 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. 21-04 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 an opinion 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 concurred with the findings identified in our engagement. The DHP's response was not subjected to the auditing procedures applied in the engagement to audit the financial statements; 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. 21-04 in considering the entity's compliance. Accordingly, this communication is not suitable for any other purpose.

Alexandria, Virginia
November 8, 2021

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Schedule of Findings

Noncompliance and Other Matters

I. The Federal Managers' Financial Integrity Act of 1982 (*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 supported 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 has not designed and implemented an effective process to assess and monitor the adequacy of its Components' internal control programs in support of the DHP Statement of Assurance. In fiscal year (FY) 2021, the DHP Enterprise's Statement of Assurance provided no assurance that internal control over operations, financial reporting, and compliance were operating effectively as of September 30, 2021.

II. The Federal Information Security Modernization Act of 2014 (*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 XI, "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 (*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*, as well as 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 are the implementation and monitoring of controls defined in NIST Special Publication (SP) 800-53, *Security and Privacy Controls for Federal Information Systems and Organizations*. The DHP deviated from recommended controls included in NIST SP 800-53, as discussed in Section XI, "Information Systems," in our *Report on Internal Control over Financial Reporting*. These deviations related to access controls, system and services acquisition, and audit and accountability, 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:

- 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*

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- Recognition and valuation requirements set forth in SFFAS No. 3, *Accounting for Inventory and Related Property*
- Liability requirements set forth in SFFAS No. 5 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*
- Accounting and reporting requirements associated with SFFAS No. 31, *Fiduciary Activities*
- 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*
- Recognition and valuation requirements set forth in SFFAS No. 44, *Accounting for Impairment of General Property, Plant and Equipment Remaining in Use*
- Accounting and reporting requirements associated with restatements per SFFAS No. 21, *Reporting Corrections of Errors and Changes in Accounting Principles*, and OMB Circular A-136, *Financial Reporting Requirements*.

United States Standard General Ledger 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 consistently account for Stockpile Materials in accordance with requirements set forth in SFFAS No. 3. The DHP recorded Stockpile Materials as

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operating expenses within the core accounting system. For additional details, see Section VIII, "Stockpile Materials" 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 completely identify capitalized expenses from non-capital expenses to appropriately record PP&E expenditures in accordance with USSGL requirements. For additional details, see Section VII, "Valuation of Property, Plant, and Equipment," in our *Report on Internal Control over Financial Reporting*
- The DHP did not consistently track and accumulate revenue and accounts receivable (AR) data to post general ledger (GL) transactions consistent with USSGL requirements. The DHP had revenue and AR 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 (*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*, the Defense Health Agency (DHA) and its Military Treatment Facilities (MTF) are not able to support the validity of debt balances associated with medical services provided, which are recorded in the DHA MTFs' 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) (*Repeat 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

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date. The following issues identified during audit procedures may represent instances of noncompliance with the ADA:

- The DHP Components and subordinate organizations, including MTFs, recorded obligations in excess of their suballotments, allocations, and suballocations. MTFs within the Service Medical Activity (SMA) – Army, SMA-Navy, and SMA-Air Force (AF), as well as funds centers within DHA, were identified that obligated more DHP funds than were suballocated to them as of March 31, 2021; $3.6 million was obligated above the amount suballocated across 49 locations. Such activity may represent violations of the ADA, as prescribed within the Assistant Secretary of Defense for Health Affairs' [ASD(HA)] policy memorandum, entitled *Formal Administrative Subdivisions of the Defense Health Program Appropriation Subject to the Antideficiency Act*. The DHP is currently assessing whether these instances represent transactional errors or noncompliance with the ADA as established by the ASD(HA) policy memorandum.

VI. The Prompt Payment Act (*New Condition*)

The Prompt Payment Act (PPA) requires Federal agencies to pay their bills on time, pay interest and penalties when payments are late, and take discounts only when payments are made within the discount period and are advantageous to the Government. 31 United States Code (U.S.C.) §3901-§3904 notes that interest penalties should be paid when agencies fail to make payments of delivered items of property or complete performance of service by the required payment date. Interest should be computed at the rate of interest established by the Secretary of the Treasury, which is in effect at the time of the accrual of the late payment interest penalty. The interest penalty shall be paid for the period beginning on the day after the required payment date and ending on the date on which payment is made. In three instances, the DHP did not demonstrate that interest was accrued or paid when invoice payment occurred after the required payment date for delivered items of property or complete performance of service.

As discussed in Section IX, "Liabilities and Related Expenses," of the *Report on Internal Control over Financial Reporting*, the DHP is not able to support the validity and existence of non-payroll expenditures. The internal control weaknesses described demonstrate an increased risk for the DHP to be fully compliant with the requirements of the PPA. The DHP's inability to sufficiently support the validity of recorded expenses limited the extent of audit procedures which could be performed over PPA requirements.

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Response to Independent Auditor's Report

OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE

1200 DEFENSE PENTAGON
WASHINGTON, DC 20301-1200

HEALTH AFFAIRS

Mr. David Zavada
Kearney and Company, P.C.
1701 Duke Street, Suite 500
Alexandria, VA 22314

Dear Mr. Zavada,

Please accept our gratitude for the Kearney and Company team's extensive efforts with the audit of the Defense Health Program (DHP) Fiscal Year (FY) 2021 financial statements. We concur with your audit results and will devise a methodical approach to design and implement corrective actions addressing your findings and recommendations.

We are in the process of refining our audit response strategy to concisely focus on remediation of material weaknesses and scope limitations. We are also working to enhance our robust Risk Management and Internal Control (RMIC) program. We acknowledge the material weaknesses identified in your "Independent Auditor' s Report on Internal Control over Financial Reporting" and the findings identified in your "Independent Auditor's Report on Compliance with Laws, Regulations, Contracts, and Grant Agreements." We will continue to work to correct, improve, and sustain progress of our accounting processes, internal controls, financial systems, and financial reporting.

We successfully remediated 37 Notices of Findings and Recommendations (NFRs) comprising 24 percent of our total NFRs. We were also able to sustain an unmodified opinion for the twelfth consecutive year for our Contract Resource Management financial statements. We will continue to proactively seek opportunities to improve the design and operating effectiveness of our financial processes, systems, and internal controls to achieve an unmodified audit opinion of our DHP financial statements.

We appreciate and extend our sincere thanks to you and your team for their professionalism, due diligence, and commitment.

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

Principal Financial Statements

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 SNC presents the net costs of operations for the four program areas established in 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 SBR provides information about DHP's budgetary resources, status of budgetary resources, and net outlays. 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, 2021 and 2020
(dollars in thousands)

	Unaudited	
Assets (Note 2)	**FY 2021**	**FY 2020**
Intragovernmental:		
Fund Balance with Treasury (Note 3)	$ 20,458,873	$ 21,988,560
Accounts Receivable, Net (Note 5)	206,059	387,739
Total Intragovernmental	$ 20,664,932	$ 22,376,299
Other than Intragovernmental/With the Public:		
Cash and Other Monetary Assets (Note 4)	$ 28	$ 1,128
Accounts Receivable, Net (Note 5)	743,679	649,162
Inventory and Related Property, Net (Note 6)	242,013	229,040
General Property, Plant, and Equipment, Net (Note 7)	3,836,160	3,435,799
Advances and Prepayments (Note 8)	13,221	8,815
Total Other than Intragovernmental/With the Public	$ 4,835,101	$ 4,323,944
Total Assets	**$ 25,500,033**	**$ 26,700,243**
Liabilities (Note 9)		
Intragovernmental:		
Accounts Payable	$ 100,315	$ 303,937
Other Liabilities (Note 12)	96,241	130,118
Total Intragovernmental	$ 196,556	$ 434,055
Other than Intragovernmental/With the Public:		
Accounts Payable	$ 1,150,948	$ 826,495
Federal Employee and Veteran Benefits payable (Note 10)	259,167,054	272,588,380
Environmental and Disposal Liabilities (Note 11)	19,633	18,378
Other Liabilities (Note 12)	271,496	313,661
Total Other than Intragovernmental/With the Public	$ 260,609,131	$ 273,746,914
Total Liabilities	**$ 260,805,687**	**$ 274,180,969**
Net Position		
Unexpended Appropriations	$ 18,522,109	$ 20,210,255
Cumulative Results of Operations	(253,827,763)	(267,690,981)
Total Net Position	**$ (235,305,654)**	**$ (247,480,726)**
Total Liabilities and Net Position	**$ 25,500,033**	**$ 26,700,243**

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, 2021 and 2020

(dollars in thousands)

	Unaudited	
	FY 2021	FY 2020
Gross Program Costs (Note 15)	**$ 38,629,154**	**$ 42,948,776**
Operations, Readiness & Support	$ 35,705,273	$ 41,021,043
Procurement	476,436	399,893
Research, Development, Test & Evaluation	2,375,781	1,730,542
Family Housing & Military Construction	71,664	(202,702)
(Less: Earned Revenue)	(3,942,225)	(4,027,367)
Net Program Costs before Losses/(gains) from Actuarial Assumption Changes for Military Retirement Benefits	**$ 34,686,929**	**$ 38,921,409**
Losses/(Gains) from Actuarial Assumption Changes for Military Retirement Benefits	$ (12,963,004)	$ 10,588,841
Net Program Costs Including Assumption Changes	$ 21,723,925	$ 49,510,250
Costs Not Assigned to Programs	-	-
(Less: Earned Revenues Not Attributable to Programs)	-	-
Net Cost of Operations	$ **21,723,925**	$ **49,510,250**

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, 2021 and 2020

(dollars in thousands)

	Unaudited FY 2021	FY 2020
Unexpended Appropriations:		
Beginning Balance	**$ 20,210,255**	**$ 18,551,635**
Budgetary Financing Sources:		
Appropriations Received	$ 34,566,142	$ 39,749,196
Appropriations Transferred-In/Out (+/-)	150,673	(1,742,308)
Other Adjustments	(796,493)	(941,843)
Appropriations Used	(35,608,468)	(35,406,425)
Total Budgetary Financing Sources	$ **(1,688,146)**	**$ 1,658,620**
Total Unexpended Appropriations	**$ 18,522,109**	**$ 20,210,255**
Cumulative Results of Operations:		
Beginning Balances	$ (267,690,981)	$ (253,340,156)
Adjustments:		
Changes in Accounting Principles (+/-)	-	830,416
Corrections of Errors (+/-)	-	-
Beginning Balances, as Adjusted	**$ (267,690,981)**	**$ (252,509,740)**
Budgetary Financing Sources:		
Appropriations Used	$ 35,608,468	$ 35,406,425
Nonexchange Revenue	2,719	26,486
Other Adjustments	7,708	28,312
Other Financing Sources:		
Transfers In/Out without Reimbursement	$ (264,763)	$ (1,380,787)
Imputed Financing	239,600	246,066
Other	(6,589)	2,507
Total Financing Sources	**$ 35,587,143**	**$ 34,329,009**
Net Cost of Operations	**$ 21,723,925**	**$ 49,510,250**
Net Change	**$ 13,863,218**	**$ (15,181,241)**
Cumulative Results of Operations	$ **(253,827,763)**	$ **(267,690,981)**
Net Position	**$ (235,305,654)**	**$ (247,480,726)**

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, 2021 and 2020

(dollars in thousands)

	Unaudited	
	FY 2021	FY 2020
Budgetary Resources		
Unobligated balance from prior year budget authority, net	$ 6,002,872	$ 4,943,590
Appropriations (discretionary and mandatory)	34,846,242	38,154,673
Spending Authority from offsetting collections (discretionary and mandatory)	4,182,735	3,953,600
Total Budgetary Resources	**$ 45,031,849**	**$ 47,051,863**
Status of Budgetary Resources		
Total New obligations and upward adjustments	$ 41,049,889	$ 41,947,437
Unobligated balance, end of year:		
Apportioned, unexpired accounts	2,574,682	3,948,860
Exempt from apportionment, unexpired accounts	128	36
Unapportioned, unexpired accounts	-	60
Unexpired unobligated balance	2,574,810	3,948,956
Expired unobligated balance	1,407,150	1,155,470
Total Unobligated balance, end of year	3,981,960	5,104,426
Total Status of Budgetary Resources	**$ 45,031,849**	**$ 47,051,863**
Outlays, net		
Total outlays, net (discretionary and mandatory)	$ 35,457,736	$ 34,619,809
Distributed offsetting receipts	-	3,129
Agency Outlays, net	**$ 35,457,736**	**$ 34,622,938**

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

DHP is a component of the U.S. Government. For this reason, some of the assets and liabilities reported by the entity may be eliminated for Government-wide reporting. These financial statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity. One implication of this is that liabilities cannot be liquidated without legislation that provides resources and legal authority to do so.

DHP is also sub-component of the DoD. The DoD includes the Office of the Secretary of Defense (OSD), Joint Chiefs of Staff (JCS), DoD OIG, Military Departments, Defense Agencies, DoD Field Activities, and CCMDs, which are considered, and may be referred to as, DoD Components. The Military Departments consist of the Departments of the Army, the Navy (of which the Marine Corps is a component), and the Air Force. The Department was established by the *National Security Act of 1947*. Since the creation of America's first army in 1775, the Department and its predecessor organizations have evolved into a global presence with a worldwide infrastructure dedicated to defending the U.S. by deterring and defeating aggression and coercion in critical regions.

In 2011, the Deputy Secretary of Defense's Task Force on Reform of the MHS led to the creation of the DHA, a Combat Support Agency (CSA) and a component of DHP. In 2013, the DoD issued a directive in accordance with the Deputy Secretary of Defense memorandum formally establishing DHA as part of DHP, which achieved full operating capability by 2015. In early 2017, in fulfillment of FY 2017 *NDAA* (P.L. 114-328), the DHA began preparing to assume responsibility for the Administration, Direction, and Control (ADC) of MTFs worldwide. The Deputy Secretary of Defense directed ADC of all MTFs and DTFs in the fifty United States and Puerto Rico transfer from the Military Departments to the DHA effective October 25, 2019. 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 six financial reporting entities that exist within DHP. These six 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, *Reporting Entity*, 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 DHP will be discussed in Note 19, Disclosure Entities and Related Parties. 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 DHP.

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 six financial reporting components comprise DHP Financial Statement Reporting Entity (FSRE):

MEDCOM: MEDCOM is a major command of the U.S. Army that provides oversight, command and control of the Army's medical readiness programs, fixed-facility medical, dental, and veterinary treatment facilities, medical research and development and training institutions.

Effective FY 2020, the Army Medical Department Center & School (AMEDDC&S) transitioned to the Army's Training and Doctrine Command. The Medical Research and Development Command (MRDC) was aligned under Army Futures Command (AFC) and medical logistics functions were transitioned to the Army Materiel Command (AMC). These organizations continue to receive DHP funding distributed through Army MEDCOM/Office of the Surgeon General (OTSG) and are included as a part of DHP Financial Statements and thus are accounted for within the consolidation entity.

BUMED: BUMED is a global healthcare network of highly trained medical personnel who provide healthcare support to the U.S. Navy, Marine Corps, their families, and veterans in high operational tempo environments, at expeditionary medical facilities, military medical treatment facilities, hospitals, clinics, hospital ships and research units around the world. BUMED is led by the Navy Surgeon General and its headquarters is the BUMED in Falls Church, VA. BUMED 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 DHP and coordinated by the Office of ASD(HA) with support from the DHA.

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

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 $45 billion DHP budgetary resources to support the delivery of integrated, affordable, and high-quality health services to the DoD's 9.6 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.

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. DHP acknowledges the existence of the museum, however a current *GAAP* Departure is also acknowledged in Note 1C of DHP AFR for the lack of Stewardship reporting of the Museum in the financial statements of DHA and DHP under Stewardship Property Reporting Requirements.

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.

Also, USUHS is a health science university of the U.S. federal government under DoD. The university consists of the F. Edward Hébert School of Medicine, a medical school, which includes a full health sciences graduate education program, the Daniel K. Inouye Graduate School of Nursing, the Postgraduate Dental College, and the College of Allied Health Sciences

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.

COVID-19

On March 27, 2020, the *Coronavirus Aid, Relief and Economic Security Act (CARES Act)* (P.L. 116-136) was signed into law, which provides FY2020 supplemental appropriations for federal agencies to respond to COVID-19. The supplemental appropriations are designated as emergency spending, which is exempt from discretionary spending limits. DHP was appropriated approximately $3.8 billion to prevent, prepare for, and respond to COVID-19, including to provide additional funds to maintain normal operations and cover other necessary authorized activities domestically or internationally during the period that the programs are impacted by the COVID-19.

On April 10, 2020, the Office of Management and Budget (OMB) issued implementation guidance for supplemental funding provided in response to the COVID-19. In balancing speed with transparency, OMB Memorandum M-20-21 directed agencies to leverage and continue to employ existing financial transparency and accountability mechanisms wherever possible. OMB M-20-21 further instructed agencies to consider three core principles: (1) mission achievement, by using data and evidence to meet program objectives; (2) expediency in issuing awards to meet crucial needs; and (3) transparency and accountability to the public.

1.B. Basis of Accounting and Presentation

Basis of Accounting and Presentation: DHP's FY ends September 30. 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 *GMRA of 1994*, and other appropriate legislation. The financial statements have been prepared from the books and records of DHP in accordance with, and to the extent possible, *GAAP* promulgated by the *FASAB*; OMB Circular A-136, *Financial Reporting Requirements*; and the *DoD's FMR*.

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

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 *GAAP*. These systems were not designed to collect and record financial information on the full accrual accounting basis as required by *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 *GAAP*. Although the DoD's continued effort towards full compliancy with *GAAP* for the accrual method of accounting is encumbered by various systems limitations and the sensitive nature of Departmental activities, DHP continues to implement process and system improvements addressing these limitations.

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.

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.

DHP in coordination with DoD Office of the OUSD(C) is continuing to evaluate the effects that will result from fully adopting recent accounting standards and other authoritative guidance issued by *FASAB*. The pronouncements listed below are expected to have an impact on DHP's financial statements; however, DHP is currently unable to determine the full impact.

- SFFAS 48, *Opening Balances for Inventory, Operating Materials and Supplies, and Stockpile Materials*: Issued on January 27, 2016; Effective for periods beginning after September 30, 2016. DHP plans to utilize deemed cost to value beginning balances for inventory and related property (I&RP), as permitted by *SFFAS 48*. DHP has valued some of its I&RP using deemed cost methodologies as described in *SFFAS 48*. However, systems required to account for historical cost for I&RP in accordance with SFFAS 3, *Accounting for Inventory and Related Property*, are not yet fully implemented. Therefore, DHP is not making an unreserved assertion with respect to this line item.
- SFFAS 50, *Establishing Opening Balances for General Property, Plant, and Equipment: Amending SFFAS 6, 10, and 23, and Rescinding SFFAS 35*: Issued August 4, 2016; Effective for periods beginning after September 30, 2016.

  DHP plans to utilize deemed cost to value beginning balances for general property, plant, and equipment (GPP&E), as permitted by *SFFAS 50*. However, systems required to account for historical cost for GPP&E in accordance with SFFAS 6, *Accounting for Property, Plant and Equipment*, are not yet fully implemented. Therefore, DHP is not making an unreserved assertion with respect to this line item.
- SFFAS 53, *Budget and Accrual Reconciliation: Amending SFFAS 7 and 24, and Rescinding SFFAS 22*: Issued October 27, 2017; Effective for periods beginning after September 30, 2018. Currently, DHP is unable to determine the exact cause of the reconciling difference in its budget and accrual reconciliation.
- SFFAS 54, *Leases: An Amendment of SFFAS 5, Accounting for Liabilities of the Federal Government and SFFAS 6*: Issued April 17, 2018; Effective for periods beginning after September 30, 2023 (as amended by *SFFAS 58*). Early adoption is not permitted.
- *FASAB* Interpretation of SFFAS 9, *Cleanup Cost Liabilities Involving Multiple Component Reporting Entities: An Interpretation of SFFAS 5 & 6*: Issued August 16, 2019; Effective for periods beginning after September 30, 2019. Early adoption is permitted.
- Technical Bulletin 2017-1, *Intragovernmental Exchange Transactions*: Issued November 1, 2017; Effective upon issuance.
- Technical Bulletin 2017-2, *Assigning Assets to Component Reporting Entities*: Issued November 1, 2017; Effective upon issuance.
- Technical Bulletin 2020-1, *Loss Allowance for Intragovernmental Receivables*: Issued February 20, 2020; Effective upon issuance.
- Technical Bulletin 2006-1, *Recognition and Measurement of Asbestos-Related Cleanup Costs*.
- Technical Release 18, *Implementation Guidance for Establishing Opening Balances*: Issued October 2, 2017; Effective upon issuance.
- Staff Implementation Guidance 6.1: *Clarification of Paragraphs 40-41 of SFFAS 6, As Amended*: Issued July 17, 2018; Effective upon issuance.

Elimination of Intra-Entity Transactions and Balances: Accounting standards require an entity to eliminate intra-entity activity and balances from consolidated financial statements 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. In accordance with the *Financial Management Requirements for Trading Partner Eliminations* Memorandum (FPM 19-03), 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: 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. 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: SFFAS 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. Accounting standards require an entity to eliminate intra-entity activity and balances from consolidated financial statements to prevent overstatement caused by the inclusion of business activity between entity components.

Treasury Financial Manual (TFM), Volume I, Part 2, Chapter 4700, also provides guidance for reporting and reconciling intragovernmental balances.

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 non-federal 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. 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. 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: 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 GAAP

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

Fund Balance with Treasury (Note 1.H. and Note 3): DHP was not able to identify its undistributed collections and disbursements in a timely manner because DHP shares a Treasury Index (TI)-97 with Other Defense Organizations (ODO) for Treasury reporting. In addition, DHP was not able to record and report transactions in suspense accounts since suspense balances are not included in FBwT balances. As a result, 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*.

Accounts Receivable, Net and Revenue Recognition (Notes 1.E. and 1.K. and Note 5): DHP did not have compliant processes in place to account for accounts receivable and the related revenue balances in accordance with *SFFAS 1*, and *SFFAS 7*, *Accounting for Revenue and Other Financing Sources*. DHP recorded accounts receivable and associated revenue upon the receipt of cash, instead of when

earned. Additionally, 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.

DHP did not have a formal policy and procedures in place to estimate the allowance for uncollectible accounts receivable in accordance with *SFFAS 1* and Technical Bulletin 2020-1, *Loss of Allowance for Intragovernmental Receivables*.

Inventory and Related Property, Net (Note 1.F., 1.L., and Note 6): 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*.

In addition, inventory and related property beginning balances have not been established using deemed cost as permitted by *SFFAS 48*.

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

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* and SFFAS 10, *Accounting for Internal Use Software*.

DHP also did not have compliant processes in place to record CIP and is currently not assessing projects to determine if there are capitalizable construction costs in accordance with *SFFAS 6*.

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.N., Note 13): DHP did not have compliant processes in place to account for capital and operating leases in accordance with *SFFAS 5*, *SFFAS 6*, and *SFFAS 10*.

Stewardship Property, Plant, and Equipment (Note 1.O.): 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.P.): DHP did not have compliant processes in place to account for accounts payable, accruals, and the related expenses in accordance with *SFFAS 1*, and *SFFAS 5*.

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

Federal Employees' Compensation Act (FECA) Liabilities (Note 1.P. and Note 10): DHP did not report the FECA actuarial liabilities/expenses and chargeback billings in accordance with *SFFAS 5*.

Environmental and Disposal Liabilities (Note 1.P. and Note 11): 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*, *SFFAS 6*, and Federal Financial Accounting and Auditing Technical Release 2, *Determining Probable and Reasonably Estimable for Environmental Liabilities in the Federal Government*.

Commitments and Contingencies (Note 1T. and Note 14): 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* and SFFAS 12, *Recognition of Contingent Liabilities Arising from Litigation*: An Amendment of *SFFAS 5*. Further, DHP did 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, 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*.

DHP is still in the process of evaluating whether 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*.

Consolidated Statements of Net Cost (Note 1.W. and Note 15): 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: DHP did not have compliant processes in place to account for intragovernmental transactions by customer in accordance with *SFFAS 4*, *SFFAS 7*, and *SFFAS 55*, 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: 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: DHP did not have compliant processes in place to account for Upward Adjustments of Prior-Year Undelivered Orders (UDO) or adjust obligations for fluctuations in price in accordance with *SFFAS 7*.

Non-Federal Physical Property: 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.

Prior Period Adjustment: DHP did not record opening balance adjustments, classified as prior period adjustments, in compliance with SFFAS 21, *Reporting Corrections of Errors and Changes in Accounting Principles*, or in compliance with presentation and disclosure requirements of *OMB Circular A-136*.

1.D. Appropriations and Funds

Appropriations: 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. DHP uses these appropriations and funds to execute its missions and subsequently report on resource usage.

Deposit Funds: 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 DHP funds and as such, are not available for DHP operations. 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). 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

As a component of the Government-wide reporting entity, DHP is subject to the Federal budget process, which involves appropriations that are provided annually. The financial transactions that are supported by budgetary resources, which include appropriations, are generally the same transactions reflected in agency and the Government-wide financial reports.

DHP's budgetary resources reflect past congressional action and enable the entity to incur budgetary obligations, but they do not reflect assets to the Government as a whole. Budgetary obligations are legal obligations for goods, services, or amounts to be paid based on statutory provisions (e.g., Social Security benefits). After budgetary obligations are incurred, Treasury will make disbursements to liquidate the budgetary obligations and finance those disbursements in the same way it finances all disbursements, using some combination of receipts, other inflows, and borrowing from the public (if there is a budget deficit).

Exchange and Non-exchange Revenue: DHP classifies revenue as either exchange revenue or non-exchange revenue. Exchange revenue is derived from transactions in which 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 DHP operations and is therefore reported on the Consolidated Statements of Changes in Net Position as a financing source. Non-exchange 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 DHP's operating funds are provided by congressional appropriations of budgetary authority. DHP receives appropriations on annual, multiple FY, and no-year bases. Upon expiration of an annual or multiple FY 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 FY appropriations are canceled at the end of the fifth FY 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. 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 DHP are paid in full or in part by funds appropriated to other federal entities. 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).

DHP has implemented *SFFAS 55*. *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. Imputed financing represents the cost paid on behalf of DHP by another federal entities. In accordance with *SFFAS 55*, the DoD 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 that are paid from the Treasury Judgement Fund. Unreimbursed costs of goods and services other than those identified above are not included in DHP's financial statements. 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, DHP does not report the consolidated support provided by U.S. allies for common defense and mutual security on the Consolidated SNC and in *Note 18, Reconciliation of Net Cost to Net Outlays*.

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

DHP acknowledges a departure from *GAAP* in its Revenue Recognition.

1.F. Recognition of Expenses

For financial reporting purposes, DoD policy requires that 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 to 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 DHP, OM&S encompasses pharmaceuticals, pharmaceutical medical supplies, and non-pharmaceutical medical supplies. Under provisions of *SFFAS 3*, DHP expenses OM&S using the purchase method of accounting. Under the consumption method, OM&S would be expensed when consumed.

1.G. Transactions with Foreign Governments and International Organizations

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

FBwT is an asset of a DHP and a liability of the U.S. Government General Fund. In both cases, the amounts represent commitments by the Government to provide resources for particular programs, but they do not represent net assets to the Government as a whole.

When DHP seeks to use FBwT to liquidate budgetary obligations, Treasury will finance the disbursements in the same way it finances all other disbursements, using some combination of receipts, other inflows, and borrowing from the public (if there is a budget deficit)

The U.S. Treasury Department performs cash management activities for all Federal Government agencies. FBwT represents DHP's right to draw funds from the Treasury for allowable expenditures. FBwT also represents the aggregate amount of DHP's available budget spending authority available to pay current liabilities and finance future authorized purchases. 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 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 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 disbursing offices of 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 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.

FBwT and the accompanying liability for deposit funds are not reported by individual Other Defense Organizations General Fund, but rather reported in the consolidated Other Defense Organizations General Fund. As such, DHP does not report deposit fund balances on its financial statements.

DHP acknowledges a departure from *GAAP* in its undistributed collections and disbursements.

For additional information, see *Note 3, Fund Balance with Treasury*.

1.I. Cash and Other Monetary Assets

Cash is the total of cash resources under the control of DHP, including coins, paper currency, negotiable instruments, and amounts held for deposit in banks and other financial institutions. Foreign currency consists of the total U.S. dollar equivalent of foreign currency exchanged for U.S. dollars and foreign currency received as payment for goods or services. Foreign currency is valued using the Treasury prevailing rate of exchange. The TFM Volume I, Part 2, Chapter 3200, provides guidance for accounting and reporting foreign currency.

The majority of cash and all foreign currency is classified as "non-entity" and is restricted. Amounts reported consist primarily of cash and foreign currency held by disbursing officers to carry out their paying, collecting, and foreign currency accommodation exchange missions.

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 FY by OUSD(C). Foreign currency fluctuations related to other appropriations require adjustments to the original obligation at the time of payment. DHP does not separately identify currency fluctuation transactions on its financial statements.

For additional information, see *Note 4, Cash and Other Monetary Assets*.

1.J. 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.

DHP acknowledges a departure from *GAAP* in its FBwT.

1.K. Accounts Receivable, Net

Accounts receivable are amounts due to DHP from other federal entities or the public.

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 calculates a separate allowance percentage for debts against suspended pharmacies. DHP's other components did not have formal policies and procedures in place to estimate the allowance for uncollectible accounts receivable

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 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, DHP will close out the bad debt and take it off their books.

DHP acknowledges a departure from *GAAP* in its Accounts Receivable, Net.

For additional information, see *Note 5, Accounts Receivable*.

1.L. Inventory and Related Property, Net

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. DHP is required to maintain various medications for the DoD in the event a medical epidemic reaches the United States. DHP accounts for the purchase of stockpile materials using the purchase method of accounting and expenses these items upon purchase instead of when consumed.

DHP acknowledges a departure from *GAAP* in its Inventory and Related Property.

For additional information, see in *Note 1.F, Recognition of Expenses* and *Note 6, Inventory and Related Property*.

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

DHP has efforts ongoing to address difficulties in determining the completeness and accuracy of reported balances and providing support for all asset costs in accordance with *SFFAS 4*, *SFFAS 6*, and and/or *SFFAS 10*. Also, DHP does not yet have *SFFAS 6* and *SFFAS 10* compliant go-forward processes, supportable GPP&E beginning balances have not been established, and DHP management has not made its unreserved assertion in accordance with *SFFAS 50*.

Capitalization Threshold: DHP's 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 (years)
Buildings, Structures, and Facilities	SL*	35, 40 or 45
Software	SL	2-5 or 10
Equipment	SL	5

*Straight line (SL)

Buildings, structures, and facilities: Real property in the federal government generally includes land, land improvements, buildings, facilities, and structures. DHP does not own land or land improvements. However, for buildings, facilities, and structures, OUSD(C) directed 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.

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

Construction-in-Progress (CIP): DoD 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. 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: DHP has not fully developed and executed its accounting policy and related reporting requirements for its lease activity. DHP is in the process of performing an analysis of its lease contracts, but that process has not yet been completed as of September 30, 2021.

DHP acknowledges a departure from *GAAP* in its General Property, Plant, and Equipment, Net.

For additional information, see *Note 7, General Property, Plant and Equipment*.

1.N. Other Assets

Advances and Prepayments: When advances are permitted by law, legislative action, or presidential authorization, 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. DHP's policy is to expense and/or properly classify assets when the related goods and services are received.

For additional information, see *Note 8, Other Assets*.

1.O. Stewardship Property, Plant, and Equipment

Disclosures for stewardship property, plant, and equipment are required under *SFFAS 29*. 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. DHP operates the National Museum of Health and Medicine.

DHP acknowledges a departure from *GAAP* in its Stewardship PP&E.

1.P. Liabilities

Liabilities represent probable and measurable amounts to be paid by 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 not covered by budgetary resources, for example future environmental cleanup liability, represent amounts owed in excess of available appropriated funds or other amounts, where there is no certainty that the appropriations will be enacted.

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: DHP segregates its other liabilities between current and noncurrent liabilities. The current liabilities represent liabilities that 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 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 DHP. These liabilities are not covered by budgetary resources because funding has not been made available.

In addition, 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: 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.

DHP acknowledges a departure from *GAAP* in its Accounts Payable, FECA Liabilities, and Environmental Liabilities.

For additional information, see *Note 9, Liabilities Not Covered by Budgetary Resources*.

1. Q. Military Retirement and Other Federal Employment Benefits

Federal Employee and Veteran Benefits Payable 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.

DHP implemented requirements of *SFFAS 33*, 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, 2020, financial statement valuation, the application of *SFFAS 33* required DoD OACT to set the long-term inflation, the Consumer Price Index (CPI), DHP actuarial liability is adjusted at the end of each FY. The 4th Quarter, FY 2021 balance represents the September 30, 2021 amount that will be effective through 3rd quarter of FY 2022.

For additional information, *see Note 10, Federal Employee and Veteran Benefits Payable*.

1.R. Accrued Unfunded Annual Leave

Accrued leave includes salaries, wages, and other compensation earned by employees, but not disbursed as of September 30, 2021. 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.

DHP acknowledges a departure from *GAAP* in its Accrued Unfunded Annual Leave.

1.S. Other Liabilities

SFFAS 51, *Insurance Programs*, established accounting and financial reporting standards for insurance programs. Office of Personnel Management (OPM) administers insurance benefit programs available for coverage to the DoD's civilian employees. The programs are available to Civilian employees, but employees do not have to participate. These programs include life, health, and long-term care insurance.

The life insurance program, Federal Employee Group Life Insurance (FEGLI) plan is a term life insurance benefit with varying amount of coverage selected by the employee. The Federal Employees Health Benefits (FEHB) program is comprised of different types of health plans that are available to Federal employees for individual and family coverage for healthcare. Those employees meeting the criteria for coverage under FEHB may also enroll in the Federal Employees Dental and Vision Insurance Program (FEDVIP). FEDVIP allows for employees to have dental insurance and vision insurance to be purchased on a group basis.

The Federal Long-Term Care Insurance Program (FLTCIP) provides long term care insurance to help pay for costs of care when enrolls need help with activities they perform every day, or have a severe cognitive impairment, such as Alzheimer's disease. To meet the eligibility requirements for FLTCIP, employees must be eligible to participate in FEHB. However, employees are not required to be enrolled in FEHB.

OPM as the administrating agency, establishes the types of insurance plans, options for coverage, the premium amounts to be paid by the employees and the amount and timing of the benefit received. The DoD has no role in negotiating these insurance contracts and incurs no liabilities directly to the insurance companies. Employee payroll withholding related to the insurance and employee matches are submitted to OPM.

TRICARE is a worldwide healthcare program that provides coverage for Active and Reserve Component Military Service members and their families, survivors, retirees, and certain former spouses. TRICARE brings together the military hospitals and clinics worldwide

with a network and non-network TRICARE authorized civilian healthcare professionals, institutions, pharmacies, and suppliers to provide access to healthcare services. TRICARE offers multiple healthcare plans. DHP's CRM component serves as the program manager for TRICARE, providing oversight, payment, and management of private sector care administered by contracted claims processors.

For additional information, see *Note 12, Other Liabilities* and *Note 20, Insurance Programs*.

1.T. 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*, as amended by *SFFAS 12*, 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.

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. 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.

DHP executes project agreements pursuant to the framework cooperative agreement with foreign governments. All these agreements give rise to obligations that are reported in the DoD financial statements, pursuant to legal authority, appropriated funds, and none are contingent. The DoD does not enter into treaties and other international agreements that create contingent liabilities.

DHP acknowledges a departure from *GAAP* in its Commitments and Contingencies.

For additional information, see *Note 14, Commitments and Contingencies*.

1.U. 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.

For additional information, see *Note 16, Disclosures Related to the Statement of Changes in Net Position*.

1.V. Treaties for Use of Foreign Bases

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 DHP continued use of these properties until the treaties expire. 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.W. 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. DHP current processes and systems capture costs based on appropriations groups.

In FY 2019, the DoD completed implementation of *SFFAS 55*, which rescinds SFFAS 30, *Inter-Entity Cost Implementation: Amending SFFAS 4* and *FASAB* 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*, as amended.

1.X. Tax Status

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

1.Y. Significant Events

As of Q3 FY 2021, DHA took over financial reporting procedures for MEDCOM. Additionally, on January 23, 2020, DHA memo, "Establishment of DHA Markets and Market Director Authorities," established the first four markets in DHA:

- National Capital Region
- Central North Carolina
- Coastal Mississippi
- Jacksonville

Note 2. Non-Entity Assets

As of September 30, 2021, and 2020 (dollars in thousands):

	Unaudited	
	FY 2021	FY 2020
Intragovernmental Assets		
Accounts Receivable	$ -	$ -
Total Intragovernmental Assets	**$ -**	**$ -**
Non-Entity:		
Accounts Receivable	$ 1,456	$ 1,990
Total Non-Entity Assets	$ **1,456**	$ **1,990**
Total Entity Assets	$ **25,498,577**	$ **26,698,253**
Total Assets	**$ 25,500,033**	**$ 26,700,243**

Non-entity assets are not available for use in DHP's normal operations. 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.

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

Note 3. Fund Balance with Treasury

As of September 30, 2021, and 2020 (dollars in thousands):

	Unaudited FY 2021	FY 2020
Status of Fund Balance with Treasury		
Unobligated Balance		
Available	$ 2,574,810	$ 3,948,896
Unavailable	1,407,150	1,155,530
Total Unobligated Balance	**$ 3,981,960**	**$ 5,104,426**
Obligated Balance not yet Disbursed	$ 16,925,338	$ 17,432,571
Total Status of Fund Balance with Treasury		
Non-Budgetary FBwT		
Unfilled Customer Orders without Advance	(241,632)	(167,622)
Receivables and Other	(206,793)	(380,815)
Total Non-Budgetary FBwT	$ **(448,425)**	$ **(548,437)**
Total FBwT	**$ 20,458,873**	**$ 21,988,560**

The Treasury records cash receipts and disbursements on DHP's behalf; funds are available only for the purposes for which the funds were appropriated. DHP's fund balances with treasury consist of solely appropriation accounts.

The Status of FBwT reflects the reconciliation between the budgetary resources supporting FBwT (largely consisting of Unobligated Balance and Obligated Balance Note Yet Disbursed) and those resources provided by other means. The Total FBwT reported on the Balance Sheet reflects the budgetary authority remaining for disbursements 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-Budgetary FBwT reduce budgetary resources. This amount is comprised of unfilled customer orders without advance of $241.6 million and reimbursements and other income earned and not collected of $206.8 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.

For COVID-19 disclosure related information see *Note 21, COVID-19 Activity*.

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

Note 4. Cash and Other Monetary Assets

As of September 30, 2021, and 2020 (dollars in thousands):

	Unaudited FY 2021	FY 2020
Cash		
Undeposited Collections	$ 28	$ 1,128
Total Cash	**$ 28**	**$ 1,128**

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

Note 5. Accounts Receivable, Net

As of September 30, 2021 (dollars in thousands):

	Unaudited		
	Gross Amount Due	Allowance for Estimated Uncollectibles	Accounts Receivable, Net
Accounts Receivable, Net			
Intragovernmental Receivables	$ 206,059	$ -	$ 206,059
Receivables Other than Intragovernmental/With the Public	1,090,151	(346,472)	743,679
Total Accounts Receivable	**$ 1,296,210**	**$ (346,472)**	**$ 949,738**

As of September 30, 2020 (dollars in thousands):

	Unaudited		
	Gross Amount Due	Allowance for Estimated Uncollectibles	Accounts Receivable, Net
Accounts Receivable, Net			
Intragovernmental Receivables	$ 387,739	$ -	$ 387,739
Receivables Other than Intragovernmental/With the Public	855,510	(206,348)	649,162
Total Accounts Receivable	**$ 1,243,249**	**$ (206,348)**	**$ 1,036,901**

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 Service Medical Activity (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 MTFs 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, 2021, CRM had recorded $223.4 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.

Furthermore, approximately $151 thousand in accounts receivable and interest and penalties owed to DHP from the public, was erroneously excluded from DHP's FY 2021 financial statements. The amount is reported in the DoD financial statements in other DoD Treasury Index 97 funds.

For COVID-19 disclosure related information see *Note 21, COVID-19 Activity*.

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

Note 6. Inventory and Related Property, Net

As of September 30, 2021, and 2020 (dollars in thousands):

	Unaudited	
	FY 2021	FY 2020
Inventory and Related Property		
Stockpile Materials Held in Reserve for Future Use	$ 242,013	$ 229,040
Total Inventory and Related Property	**$ 242,013**	**$ 229,040**

OM&S consist of tangible personal property to be consumed in normal operations.

Stockpile Material consist of materials held due to statutory requirements for strategic and critical material for use in national defense, conservation, or national emergencies including the National Defense Stockpile Transaction Fund.

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 $242.0 million of stockpile recorded reflects remediation efforts to record stockpile material using the consumption method of accounting as required by *SFFAS 3*.

Inventory Purchases – DHP SMA components (BUMED, MEDCOM and AFMS) do not maintain or report an inventory balance for pharmaceuticals and medical supplies. *SFFAS 3* provides the following definition for inventory "'Inventory" is tangible personal property that is (1) held for sale, (2) in the process of production for sale, or (3) to be consumed in the production of goods for sale or in the provision of services for a fee. The term "held for sale" shall be interpreted to include items for sale or transfer to (1) entities outside the federal government, or (2) other federal entities." Based on the above definition and the fact that DHP activities do not provide goods or services for a fee, DHP does not have an inventory balance in accordance with accounting standards. DHP pharmaceuticals and medical supplies are expensed upon receipt at the cost-center when received in accordance with accounting standards.

The Defense Medical Logistics Standard Support (DMLSS) Program, co-sponsored by the Assistant Secretary of Defense (Health Affairs) and the Deputy Under Secretary of Defense (Logistics), is a partnership involving the wholesale medical logistics, medical information management, medical information technology, and user communities. The DMLSS Program has achieved significant savings by implementing just-in-time practices and Prime Vendor support concepts, eliminating the need to maintain large inventories of pharmaceutical and medical/surgical items at the wholesale level and at MTFs. By providing price comparison tools and electronic commerce capabilities, DMLSS has enabled MTFs to select and order the best value item that meets their requirements.

Prime Vendor is the primary distribution channel (single distributor) for procurement and delivery of a full range of commercial "brand-specific" pharmaceuticals and medical/surgical supplies to a group of MTFs in a given geographical region. Prime Vendor also covers Europe and the Pacific. Pricing of items ordered through the Prime Vendor Program is determined by Distribution and Pricing Agreements (DAPAs) negotiated between the Defense Logistics Agency (DLA) Troop Support and the manufacturer/distributor.

Internal Control Analysis – DHP components are in preliminary stages of flowcharting and documenting processes and assessing information technology and internal control of financial reporting risk with respect to the functions of purchasing and distributing pharmaceuticals and medical supplies at MTFs. Currently, DHP SMA Components expense pharmaceutical and medical supplies when purchased and placed into operation using the Prime Vendor Program. The MTFs maintain a reorder point which would provide them with a maximum of a seven to ten-day supply. DHP SMA Components use DMLSS to manage their supply and equipment purchases. SFFAS No. 3 provides the following as it applies to the financial reporting of OM&S: "If (1) operating materials and supplies are not significant amounts, (2) they are in the hands of the end user for use in normal operations, or (3) it is not cost beneficial to apply the consumption method of accounting, then the purchases method may be applied to operating materials and supplies. The purchases method provides that operating materials and supplies be expensed when purchased. An end user is any component of a reporting entity that obtains goods for direct use in the Component's normal operations. Any component of a reporting entity, including contractors, that maintains or stocks operating materials and supplies for future issuance shall not be considered an end user." DHP activities are the end user and the pharmaceuticals and medical supplies used are consumed during normal operations. As a result, and in accordance with the accounting standards, the assets are accounted for using the purchase method and a balance is not applicable for financial reporting purposes.

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

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

As of September 30, 2021 (dollars in thousands):

	Unaudited		
	Acquisition Value	Accumulated Depreciation/ Amortization	Net Book Value
Major Fixed Asset Classes			
Buildings, Structures, and Facilities	$ -	$ -	$ -
Software	1,166,086	(683)	1,165,403
General Equipment	1,759,528	(1,354,901)	404,627
Capital Leases	3,347	(3,347)	-
Construction-in-Progress (CIP)	2,266,130	-	2,266,130
Total General Property, Plant, and Equipment	**$ 5,195,091**	**$ (1,358,931)**	**$ 3,836,160**

As of September 30, 2020 (dollars in thousands):

	Unaudited		
	Acquisition Value	Accumulated Depreciation/ Amortization	Net Book Value
Major Fixed Asset Classes			
Buildings, Structures, and Facilities	$ -	$ -	$ -
Software	1,049,145	(560)	1,048,585
General Equipment	1,679,952	(1,339,195)	340,757
Capital Leases	3,347	(3,347)	-
Construction-in-Progress (CIP)	2,046,457	-	2,046,457
Total General Property, Plant, and Equipment	**$ 4,778,901**	**$ (1,343,102)**	**$ 3,435,799**

Most of DHP's PP&E, 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.

The total PP&E and accumulated depreciation for the current year as shown in the reconciliation below.

Buildings, Structures, and Facilities

DHP facilities range from sophisticated tertiary care medical centers to outpatient and dental clinics and physiological training units. Per OUSD(C) *Real Property Financial Reporting Responsibilities Policy Update*, the Buildings, Structures and Facilities were transferred to the Military Departments that own the installations on which they reside. Refer to *Note 1.M. General Property, Plant, and Equipment, Net*.

Internal Use Software (IUS)

IUS 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.

In FY 2020, DHP recorded a prior period adjustment for Internal Use Software in Development (IUSID), as the DHP continues efforts to meet historical cost requirements prescribed by *SFFAS 10*, as amended by *SFFAS 50*. The prior period adjustment was not recorded in accordance with requirements set forth in *SFFAS 21*. The DHP acknowledges departures from *GAAP* related to prior period adjustments as discussed in *Note 1.C, Departures from GAAP*.

See *Note 18, Disclosures Related to the Statement of Changes in Net Position* for more information regarding FY 2020 IUS prior period adjustment.

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. 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 DHP 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

DHP often encounters the need to obtain fixed assets through the process of construction. Costs related to constructed assets of 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

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 use or convertibility of general property, plant, and equipment.

Depreciation and amortization expense for the year ended, September 30, 2021, totaled $108.1 million.

General PP&E, Net – Summary of Activity

General property, plant, and equipment, net consisted of the following as of September 30, 2021 and 2020 (*dollars in thousands*):

	Unaudited FY 2021	FY 2020
General PP&E, Net Beginning of Year	$ 3,435,797	$ 3,224,053
Capitalized Acquisitions	759,223	263,281
Dispositions	4,614	-
Revaluations (+/-)	10,094	1,437,465
Depreciation Expense	(108,057)	(119,004)
Transfers In/(Out) without Reimbursement	(265,511)	(1,369,996)
General PP&E, Net End of Year	$ 3,836,160	$ 3,435,799

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

Note 8. Other Assets

As of September 30, 2021, and 2020 (dollars in thousands):

	Unaudited FY 2021	FY 2020
Other than Intragovernmental/With the Public		
Advances and Prepayments	$ 13,221	$ 8,815
Total Other than Intragovernmental/With the Public	$ 13,221	$ 8,815
Less: "Advances and Prepayments"	$ (13,221)	$ (8,815)
Total Other Assets	$ -	$ -

Other assets can include those assets, such as civil service employee pay advances and travel advances that are not reported elsewhere on DHP's Balance Sheet. Advances and Prepayments, which are made in contemplation of the future performance of services, receipt of goods, incurrence of expenditures, or receipt of goods and services, are excluded from "other assets" in FY 21 as they are presented discretely on the balance sheet.

The format of the Balance Sheet has changed to reflect more detail for certain line items, as required for all significant reporting entities by OMB Circular A-136. This change does not affect totals for assets, liabilities, or net position and is intended to allow readers of this Report to see how the amounts shown on the Balance Sheet are reflected on the Government-wide Balance Sheet, thereby supporting the preparation and audit of the Financial Report of the United States Government. The presentation of the fiscal year 2020 Balance Sheet was modified to be consistent with the fiscal year 2021 presentation.

For COVID-19 disclosure related information see *Note 21, COVID-19 Activity*.

Note 9. Liabilities Not Covered by Budgetary Resources

As of September 30, 2021, and 2020 (dollars in thousands):

	Unaudited FY 2021	FY 2020
Intragovernmental		
Accounts Payable	$ 1,385	$ 1,875
Other	44,023	44,725
Total Intragovernmental Liabilities Not Covered by Budgetary Resources	**$ 45,408**	**$ 46,600**
Liabilities Other than Intragovernmental/With the Public		
Accounts payable	$ 108,365	$ 108,796
Federal employee and veteran benefits payable	259,137,923	272,565,371
Environment & Disposal Liabilities	18,098	18,098
Other Liabilities	-	677
Total Liabilities Other than Intragovernmental/With the Public Not Covered by Budgetary Resources	**$ 259,264,386**	**$ 272,692,942**
Total Liabilities Not Covered by Budgetary Resources	**$ 259,309,794**	**$ 272,739,542**
Total Liabilities Covered by Budgetary Resources	**$ 1,495,893**	**$ 1,441,427**
Total Liabilities	$ 260,805,687	$ 274,180,969

Liabilities not covered by budgetary resources are liabilities not currently funded by existing budgetary authority as of the balance sheet date. Regardless of when the congressional action occurs, when the liabilities are liquidated, Treasury will finance the liquidation in the same way that it finances all other disbursements, using some combination of receipts, other inflows, and borrowing from the public (if there is a budget deficit). 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 FECA, Judgement Fund and unemployment compensation.

Other than Intragovernmental/With the Public Liabilities – Accounts Payable

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

Other than Intragovernmental/With the Public Liabilities – Federal employee and veteran benefits payable

These consists of various employee actuarial liabilities not due and payable during the current FY. In FY 2021 these liabilities primarily consist of $256.8 billion in health benefit liabilities. Refer to *Note 10, Military Retirement and Other Federal Employment Benefits*, for additional details and disclosures.

Other than Intragovernmental/With the Public 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.

Other than Intragovernmental/With the Public – Other

Represents various contingent liability amounts booked by DHP. 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.

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

For COVID-19 disclosure related information see *Note 21, COVID-19 Activity*.

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

Note 10. Federal Employee and Veteran Benefits Payable

Federal Employee and Veteran Benefits Payable as of September 30, 2021 (dollars in thousands):

	Unaudited FY 2021	FY 2020
Pension and Health Benefits		
Military Pre Medicare-Eligible Retiree Health Benefits	$ 256,828,640	$ 270,264,694
Total Pension and Health Benefits	**$ 256,828,640**	**$ 270,264,694**
Federal Employment Benefits		
FECA	$ 177,897	$ 180,590
Other	2,160,517	2,143,096
Total Other Employee Benefits	**2,338,414**	**2,323,686**
Federal Employee and Veteran Benefits Liability	**$ 259,167,054**	**$ 272,588,380**
Other Benefit-Related Payables Included in Intragovernmental Accounts Payable on the Balance Sheet	**$** 93,235	**$** 95,574
Total Federal Employee Benefits and Veteran Benefits Payable	**$ 259,260,289**	**$ 272,683,954**

Actuarial liability as of September 30, 2021 (dollars in thousands):

	Unaudited	
	FY 2021	FY 2020
Beginning Actuarial Liability	$ 270,264,694	$ 254,832,838
Expenses		
Normal Cost	$ 12,950,853	$ 10,746,861
Interest Cost	9,166,326	9,103,914
Actuarial Experience Gains	(11,604,886)	(3,977,147)
Other Factors	(2)	1
Total Expenses before Gains from Actuarial Assumptions Changes	$ 10,512,291	$ 15,873,629
Actuarial Assumption Changes		
Changes in Trend Assumptions	$ (13,958,732)	$ 5,390,748
Changes in Assumptions Other than Trend	995,728	5,198,093
Total (gains) from Actuarial Assumption Changes	$ (12,963,004)	$ 10,588,841
Total Expenses	$ (2,450,713)	$ 26,462,470
Less: Benefit Outlays	10,985,341	11,030,614
Total Changes in Actuarial Liability	$ (13,436,054)	$ 15,431,856
Ending Actuarial Liability	$ 256,828,640	$ 270,264,694

The DoD Office of the Actuary (DoD OACT) calculates this actuarial liability at the end of each FY 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 Federal Employee and Veteran Benefits Payable. 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 ($215 thousand in FY 2021) for a closed group of USUHS retirees and the incurred-but-not-reported reserve (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).

Effective FY 2010, DHP implemented requirements of *SFFAS 33*, 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, 2021, financial statement valuation, the application of *SFFAS 33* required DoD OACT to set the long-term inflation (CPI) to be consistent with the underlying Treasury spot rates used in the valuation.

DHP actuarial liability is adjusted at the end of each FY. The 4th Quarter, FY 2021 balance represents the September 30, 2021 amount that will be effective through 3rd quarter of FY 2022.

Actuarial Cost Method: As prescribed by *SFFAS 5*, the valuation of the DHA 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 2021 financial-statement valuation, the long-term assumptions include a 3.0% discount rate and medical trend rates that were developed using a 1.6% 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 2020 financial-statement valuation, the long-term assumptions included a 3.3% discount rate and medical trend rates that were developed using a 1.6% 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 2021 "rolled-forward" actuarial liability, the following assumptions were used:

Discount Rate	3.0%	
Inflation	1.6%	
Medical Trend (Non-Medicare)	**FY 2020 – FY 2021**	**Ultimate Rate FY 2045**
Direct Care Inpatient	4.55%	3.60%
Direct Care Outpatient	5.15%	3.60%
Direct Care Prescription Drugs	-8.96%	3.60%
Purchased Care Inpatient	4.55%	3.60%
Purchased Care Outpatient	5.15%	3.60%
Purchased Care Prescription Drugs	10.61%	3.60%
Purchased Care USFHP	5.06%	3.60%

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

DHP actuarial liability decreased $13.4 billion (-5.0%). This resulted from the net effect of an increase of $11.1 billion due to expected increases (interest cost plus normal cost less benefit outlays), a decrease of $14.0 billion due to changes in key assumptions; and a decrease of $11.6 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, 2021 financial-statement valuation, DoD OACT determined a single equivalent discount rate of 3.0% 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, 2011 through March 31, 2021.

For the September 30, 2021, financial statement valuation, DoD OACT determined a single equivalent medical cost trend rate of 4.11% can be used to reproduce the total Military Retiree Health Benefits (MRHB) liability. The total MRHB liability includes Medicare-Eligible Retiree Health Care Fund (MERHCF), Service Medical Activity (SMA), and Contract Resource Management (CRM).

Note: Note 10 presented in the FY 2020 AFR does not agree one-to-one to the Note 10 presented in the FY 2021 AFR due to a change in U.S. Treasury mapping logic in its Balance Sheet Crosswalk. The change flows through to the notes for consistency.

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

Note 11. Environmental and Disposal Liabilities

As of September 30, 2021 (dollars in thousands):

	Unaudited	
	FY 2021	FY 2020
Environmental Liabilities – Other than Intragovernmental/With the Public		
Environmental Corrective Action / Closure Requirements	$ 1,536	$ 281
Nuclear Powered Military Equipment / Spent Nuclear Fuel	16,740	16,740
Other Accrued Environmental Liabilities - Non-Base Realignment and Closure (BRAC)	1,357	1,357
Total Environmental Liabilities	**$ 19,633**	**$ 18,378**

Applicable laws and regulations for cleanup requirements:

- *Comprehensive Environmental Response, Compensation, and Liability Act* (CERCLA, P. L. 96-510)
- *Superfund Amendments and Reauthorization Act* (SARA, P. L. 99-499)
- *Clean Water Act of 1977* (P. L. 95-217)
- *Safe Drinking Water Act* (P. L. 93-523)
- *Clean Air Act* (P. L. 88-206)
- *Resource Conversation and Recovery Act of 1976* (RCRA, P.L. 94-580)
- *Toxic Substances Control Act* (TSCA, P. L. 94-469)
- *Medical Waste Tracking Act of 1988* (P. L. 100-582)
- *Atomic Energy Act of 1946* (P.L. 79-585) as amended
- *Nuclear Waste Policy Act of 1982* (P. L. 97-425)
- *Low Level Radioactive Waste Policy Amendments Act of 1985* (P. L. 99-240)

DHP follows the *CERCLA*, *SARA*, *RCRA*, and 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* 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* 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 revised estimated liabilities at the end of FY 2021 are $19.6 million.

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.

DHP tangible property, plant, and equipment contains nonfriable asbestos. At this time, DHP is unable to reasonably estimate the clean-up costs related to removal and some environmental liabilities.

For DHP SMA components, the environmental liabilities and disposal liabilities cost estimation and sustainment process is owned and maintained by the Department of Navy, Department of the Army and Department of the Air Force. These Military Departments capture and record environmental liabilities allowing the environmental liabilities to be consolidated and reported on the quarterly Departments Financial Statements. As a result, BUMED, MEDCOM and AFMS report a zero balance for environmental liabilities and disposal liabilities on the quarterly financial statements.

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

There are instances when a component reporting entity recognizes General PP&E during its useful life differs from the component reporting entity that will eventually be responsible for the future outflow of resources required for cleanup when the asset is removed from service. *FASAB Interpretation 9*, clarifies during the asset's useful life the reporting entity owning the asset must continue to recognize inter-period operating costs on its Statement of Net Cost and accrue the liability for General PP&E on its Balance Sheet. When the asset is transferred to the entity designated responsible by law, statute or policy for cleanup, the General PP&E and the associated liability must be de-recognized by the component reporting entity that recognized them during the General PP&E's useful life and recognized by the component reporting entity responsible for clean-up and liquidating the liability. De-recognition and recognition of the general PP&E and liability must be performed in accordance with existing accounting standards. The Component recording the environmental liability must have sufficient supporting documentation to establish its responsibility for the liability.

Note 12. Other Liabilities

As of September 30, 2021 (dollars in thousands):

	Unaudited		
	Current Liability	Noncurrent Liability	Total
Intragovernmental			
Advances from Others	$ 1,550	$ -	$ 1,550
FECA Reimbursements due to DOL	-	-	-
Employer Contributions and Payroll Taxes Payable	-	-	-
Other Liabilities	984	472	1,456
Subtotal	**$ 2,534**	**$ 472**	**$ 3,006**
Other Liabilities reported on Note 10, *Federal Employee and Veteran Benefits Payable*	$ 93,235	$ -	$ 93,235
Total Intragovernmental Other Liabilities	**$ 95,769**	**$ 472**	**$ 96,241**
Other than Intragovernmental/With the Public			
Accrued Funded Payroll and Benefits	$ 256,661	$ -	$ 256,661
Advances from Others	7,441	847	8,288
Employer Contributions and Payroll Taxes Payable	-	-	-
Other Liabilities	-	-	-
Other Liabilities without Related Budgetary Obligations	$ 6,547	$ -	$ 6,547
Total Other than Intragovernmental/With the Public Other Liabilities	**$ 270,649**	**$ 847**	**$ 271,496**
Total Other Liabilities	**$ 366,418**	**$ 1,319**	**$ 367,737**

As of September 30, 2020 (dollars in thousands):

	Unaudited		
	Current Liability	Noncurrent Liability	Total
Intragovernmental			
Advances from Others	$ 32,554	$ -	$ 32,554
FECA Reimbursements due to DOL	-	-	-
Employer Contributions and Payroll Taxes Payable	-	-	-
Other Liabilities	764	1,226	1,990
Subtotal	**$ 33,318**	**$ 1,226**	**$ 34,544**
Other Liabilities reported on Note 10, *Federal Employee and Veteran Benefits Payable*	$ 95,574	$ -	$ 95,574
Total Intragovernmental Other Liabilities	**$ 128,892**	**$ 1,226**	**$ 130,118**
Other than Intragovernmental/With the Public			
Accrued Funded Payroll and Benefits	$ 261,287	$ -	$ 261,287
Advances from Others	45,780	883	46,663
Employer Contributions and Payroll Taxes Payable	-	-	-
Contingent Liabilities	-	678	678
Other Liabilities	-	-	-
Other Liabilities w/o Related Budgetary Obligations	5,033	-	5,033
Total Other than Intragovernmental/With the Public	**$ 312,100**	**$ 1,561**	**$ 313,661**
Total Other Liabilities	**$ 440,992**	**$ 2,787**	**$ 443,779**

Advances from Others

The balance represents liabilities for collections received to cover future expenses or acquisition of assets DHP incurs or acquires on behalf of another organization.

Federal Employees' Compensation Act Reimbursement to the DOL

The balance represents liabilities due under the FECA. The liability includes amounts for unbilled incurred and estimated accruals. Refer to *Note 10, Federal Employee and Veteran Benefits Payable*, for the estimated FECA actuarial liability.

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

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 and benefits $256.7 million 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.

For COVID-19 disclosure related information see *Note 21, COVID-19 Activity*.

Note 13. Leases

Capital Leases

As of September 30, 2021 (dollars in thousands):

	Unaudited FY 2021	FY 2020
Entity as Lessee - Capital Leases		
Land and Buildings	$ -	$ -
Machinery and Equipment	3,347	3,347
Other	-	-
Accumulated Amortization	(3,347)	(3,347)
Total Assets Under Capital Leases	$ -	$ -

DHP is reporting capital lease equipment and related amortization related to a BUMED arrangement that is covered by budgetary resources, allowing BUMED access to digital radiographic systems and full body computed tomography scanning systems.

Future Payments Due for Federal and Non-Federal Capital Leases:

DHP currently has no significant capital leases payments with terms longer than one year.

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

There are two reasonably possible cases or claims pending with DHP meeting the requirements for disclosure.

- **4DD Holdings, LLC and T4 Data Group, LLC v. United States (Court of Federal Claims)**. Plaintiffs allege infringement of its copyrights by cloning, copying, and installing 4DD's proprietary software program - TETRA® Healthcare Federator ("TETRA) – on servers and other computing devices with thousands of processor cores for which licenses were not purchased. The Complaint was filed on August 28, 2015, and an Amended Complaint on March 14, 2016. The Government filed its Answers. On June 24, 2016, the Government filed a partial Motion to Dismiss for Lack of Jurisdiction, which the Court denied near the close of discovery on April 23, 2019. On the same day, the Court granted plaintiffs' motion for sanctions upon finding that the Government failed to properly preserve relevant evidence. Both parties filed motions for summary judgment. The Court recently re-opened expert discovery to allow the Government to depose plaintiff's expert. The estimated amount or range of potential loss is $1-5 billion.
- **Bio-Medical Applications of Georgia, Inc., et al. v. United States (Court of Federal Claims)**. Plaintiffs challenge the DHA's payment methodology for End Stage Renal Disease dialysis treatments at freestanding dialysis facilities. Plaintiffs filed the Complaint on June 28, 2019. The Complaint alleges breach of contract, breach of the covenant of good faith and fair

dealings, and violations of a money-mandating regulation. On April 16, 2020, in an oral ruling, the Court of Federal Claims granted the Government's Motion to Dismiss in part and dismissed Counts II (breach of contract) and III (breach of the covenant of good faith and fair dealings). The Government filed its Answer on July 8, 2020, and discovery is ongoing. Plaintiffs recently amended its Complaint alleging that the Government illegally invoked a Government debt recovery process to take approximately $12.5 million from Plaintiffs, increasing the potential liability exposure by the same amount. The Government filed its Answer on October 14, 2021. The parties will complete discovery in January 2022. The estimated amount or range of potential loss is unknown.

Furthermore, medical malpractice claims and settlements arising from the activities of the 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.

For COVID-19 disclosure related information see *Note 21, COVID-19 Activity*.

The table below summarizes DHP's probable and reasonably possible contingent liabilities as of September 30, 2021 and 2020:

As of September 30, 2021 (dollars in thousands):

	Unaudited		
		Estimated Range of Loss	
	Accrued Liabilities	Lower End	Upper End
Legal Contingencies			
Probable	$ -	$ -	$ -
Reasonably Possible	$ -	$ 1,000,000	$ 5,000,000

As of September 30, 2020 (dollars in thousands):

	Unaudited		
		Estimated Range of Loss	
	Accrued Liabilities	Lower End	Upper End
Legal Contingencies			
Probable	$ -	$ -	$ -
Reasonably Possible	$ -	$ 1,000,000	$ 5,000,000

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

Note 15. Disclosures Related to the Statements of Net Cost

As of September 30, 2021 (dollars in thousands):

	Unaudited FY 2021	FY 2020
Program Costs		
Operations, Readiness and Support		
Gross Costs	$ 35,705,273	$ 41,021,043
Less: Earned Revenue	(3,915,809)	(4,012,013)
Losses/(Gains) from Adjustments due to changes in Actuarial Assumptions	(12,963,004)	10,588,841
Net Program Cost	**$ 18,826,460**	**$ 47,597,871**
Procurement		
Gross Cost	$ 476,436	$ 399,893
Less: Earned Revenue	(16,791)	(2,791)
Net Program Cost	**$ 459,645**	**$ 397,102**
Research, Development, Test and Evaluation		
Gross Cost	$ 2,375,781	$ 1,730,542
Less: Earned Revenue	(9,625)	(12,563)
Net Program Cost	**$ 2,366,156**	**$ 1,717,979**
Family Housing and Military Construction		
Gross Cost	$ 71,664	$ (202,702)
Less: Earned Revenue	-	-
Net Program Cost	**$ 71,664**	**$ (202,702)**
Total Gross Costs	**$ 38,629,154**	**$ 42,948,776**
Less: Total Earned Revenue	**$ (3,942,225)**	**(4,027,367)**
Changes for Military Retirement Benefits	**(12,963,004)**	**10,588,841**
Net Cost of Operations	**$ 21,723,925**	**$ 49,510,250**

DHP's current processes and systems capture costs based on appropriations groups as presented in the schedule above. DHP is in the process of reviewing available data and developing a cost reporting methodology required by the *SFFAS 4*, as amended by *SFFAS 55*. DHP implemented *SFFAS 55* in FY 2018 which rescind *SFFAS 30,* and *FASAB Interpretation 6*.

DHP's Military Retirement and post-employment costs are reported in accordance 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 benefits and other postemployment benefits on the SNC.

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

Exchange Revenue

DHP has not disclosed exchange revenue pricing and loss information in accordance with *SFFAS 7*, paragraph 46 since DHP uses full cost or market pricing for all exchange transactions.

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.

For COVID-19 disclosure related information see *Note 21, COVID-19 Activity*.

Note 16. Disclosures Related to the Statement of Changes in Net Position

DHP recorded a prior period adjustment in FY 2020, which was presented as a change in accounting principle. The prior period adjustment, associated with valuation efforts of PP&E as further discussed in Note 7, adjusted the beginning balance of cumulative results of operations by $830 million.

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

Note 17. Disclosures Related to the Combined Statement of Budgetary Resources

Disclosures related to the *SBR* consisted of the following as of September 30, 2021 and 2020:

Undelivered Orders at End of the Period

Undelivered orders 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. 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 end of FY 2021, consisted of:

As of September 30, 2021 (dollars in thousands):

	Unaudited	
	FY 2021	FY 2020
Undelivered Orders		
Intragovernmental:		
Undelivered Orders – Unpaid	$ 1,389,745	$ 4,660,443
Total Intragovernmental Undelivered Orders	$ 1,389,745	$ 4,660,443
Other than Intragovernmental/With the Public:		
Undelivered Orders – Unpaid	$ 14,051,870	$ 11,410,048
Undelivered Orders – Paid	13,221	8,815
Total Undelivered Orders Other than Intragovernmental/With the Public	$ 14,065,091	$ 11,418,863
Total Undelivered Orders	$ 15,454,836	$ 16,079,306

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 FY 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 FY 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 Combined 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 2020 balances. The budget with FY 2021 actual values and will be available at a later date at https://www.whitehouse.gov/omb/budget.

Budget of the U.S. Government

(dollars in thousands)	Budgetary Resources	New Obligations & Upward Adjustments	Distributed Offsetting Receipts	Net Outlays, Net
Combined Statement of Budgetary Resources	$ 47,051,863	$ 41,947,437	$ 3,129	$ 34,622,938
Shared Appropriations with Others included in the SBR but excluded from DHP direct appropriations presented in the President's Budget	(1,117,756)	(500,475)	-	(526,402)
Unobligated Balance Brought Forward from prior year included in the SBR but not included in the President's Budget	(1,587,027)	-	-	-
Other	(96,080)	38	(3,129)	(2,536)
Budget of the U.S. Government	**$ 44,251,000**	**$ 41,447,000**	**$ -**	**$ 34,094,000**

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.

Governmentwide Treasury Account Symbol (GTAS) Reporting Variance

DHP had an abnormal balance at the GTAS reporting level as of September 30, 2021, resulting from an error in recording a FY 2015 civilian payroll disbursement. This error prevented DHP appropriation for FY 2015-2016 from appropriately closing in FY 2021 as the funds have been canceled. An adjustment made during the FY 2021 GTAS revision period was necessary to properly close the funds with the U.S. Treasury. These funds are not reported in the FY 2021 financial statements because the FY 2015-2016 funds became unavailable for DHP use at the end of FY 2021.

For COVID-19 disclosure related information see *Note 21, COVID-19 Activity*.

Note 18. Reconciliation of Net Cost to Net Outlays

SFFAS 53 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. The analysis only displays information for the reporting period for the Year Ended September 30, 2021.

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, 2021 (dollars in thousands):

	Unaudited FY 2021 Intragovernmental	With the Public	Total
Net Operating Cost	$ 443,979	$ 21,279,946	$ 21,723,925
Components of Net Cost That are not Part of Net Outlays			
Property, Plant, and Equipment net change	$ -	$ 400,363	$ 400,363
Increase/(Decrease) in Assets:			
Accounts Receivable	$ (177,380)	$ 94,517	$ (82,863)
Other Assets	-	3,305	3,305
(Increase)/Decrease in Liabilities			-
Accounts Payable	$ 201,660	$ (324,452)	$ (122,792)
Environmental and Disposal Liabilities	-	(1,255)	(1,255)
Federal employee and veteran benefits payable	-	13,421,326	13,421,326
Other Liabilities	31,538	42,165	73,703
Other Financing Sources			
Imputed cost	$ (239,600)	$ -	$ (239,600)
Financing Sources Transferred In/out without reimbursement	264,762	-	264,762
Total Components of Net Costs that Are Not Part of Net Outlays	$ 80,980	$ 13,635,969	$ 13,716,949
Components of Net Outlays That are not Part of Net Costs			
Acquisition of Capital Assets	$ -	$ -	$ -
Inventories and related property	-	12,973	12,973
Other	-	-	-
Total Components of Net Outlays That are not Part of Net Costs	$ -	$ 12,973	$ 12,973
Net Outlays	$	$	$ 35,453,847
Agency Outlays, Net, From Statements of Budgetary Resources			$ 35,457,736
Unreconciled Difference			$ (3,889)

As of September 30, 2020 (dollars in thousands):

	Unaudited FY 2020 Intragovernmental	With the Public	Total
Net Operating Cost	$ 2,962,207	$ 46,548,043	$ 49,510,250
Components of Net Cost That are not Part of Net Outlays			
Property, Plant, and Equipment Net Change	$ -	$ 211,745	$ 211,745
Increase/(Decrease) in Assets:			
Accounts Receivable	$ 165,320	$ (88,592)	$ 76,728
Other Assets	-	(23,372)	(23,372)
(Increase)/Decrease in Liabilities			
Accounts Payable	$ (131,589)	$ 106,108	$ (25,481)
Environmental and Disposal Liabilities	-	(281)	(281)
Federal employee and veteran benefits payable	-	(15,541,908)	(15,541,908)
Other Liabilities	(16,753)	(23,401)	(40,154)
Other Financing Sources			
Imputed cost	$ (246,066)	$ -	$ (246,066)
Transfers Out/(In) Without Reimbursement	1,380,787	-	1,380,787
Total Components of Net Costs that Are Not Part of Net Outlays	$ 1,151,699	$ (15,359,701)	$ (14,208,002)
Components of Net Outlays That are not Part of Net Costs			
Acquisition of Capital Assets	$ -	$ -	$ -
Inventories and related property	-	176,970	176,970
Other	-	(1,440,174)	(1,440,174)
	3,129	-	3,129
Total Components of Net Outlays That are not Part of Net Costs	$ 3,129	$ (1,263,204)	$ (1,260,075)
Net Outlays	$ 4,117,035	$ 29,925,138	$ 34,042,173
Agency Outlays, Net, From Statements of Budgetary Resources			$ 34,622,938
Unreconciled Difference			$ (580,765)

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 DHP. Research is on-going, with coordination from DFAS, to resolve the remaining difference.

Note 19. Disclosure Entities and Related Parties

DHP has implemented *SFFAS 47*. 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 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 2020 are consistent with accounts reported within DHP financial statements for FY 2021. 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 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 DHP, to the potential risk of misuse or improper accounting treatment of these funds while in the possession of HJF.

DoD receives significant benefits from the work of the FFRDCs, which is critical to national security. Congress restricts the amount of support that the Department may receive from DoD-sponsored FFRDCs through a limitation that it sets annually on the staff years of technical effort that may be funded.

DHP also identified nine disclosure activities:

DoD Acquisition Workforce Development Fund, Transfer Account

The DoD Acquisition Workforce Development Fund (DAWDF) was established under *10 U.S.C. § 1075*. The law requires that not more than 30 days after the end of the first quarter of each FY, 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 FY. The applicable percentage for a FY is the percentage that results in the credit to the Fund of $500,000,000 in such FY. 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 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 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 P.L. 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. DHP can partake in these initiatives and as such is afforded the potential to obtain these same benefits. DHP transferred $15 million in funding to this program during FY 2021.

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 President's Emergency Plan for AIDS Relief (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 ($307k) transferred to them using the 2X fund code to support two GS Personnel at DIMO warranting disclosure within 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 to construct new houses for families on the sites of MTFs and VA medical centers.

Federally Funded Research and Development Centers (FFRDCs)

DoD maintains contractual relationships with the parent organizations of ten DoD-sponsored FFRDCs to meet some special research or development needs that cannot be met as effectively by existing government or contractor resources. The work performed by the FFRDCs provide benefits to DoD, which support national security. FFRDCs that provide support to DoD are classified into three categories:

- Research and Development Laboratories,
- Systems Engineering and Integration Centers, and
- Study and Analysis Centers.

FFRDC relationships are defined through a bi-lateral sponsoring agreement between each DoD sponsoring organization and the parent organization that operates each FFRDC. All DoD funding for FFRDC work is provided through the Department's contract with the FFRDC's parent organization. While DoD does not control the day-to-day operations of the FFRDCs, the parent organization must agree that the FFRDC will conduct its business in a manner befitting its special relationship with DoD, operate in the public interest with objectivity and independence, and be free from organizational conflicts of interest.

DoD does not have an ownership interest in the FFRDCs and is not exposed to the benefits of gains or risk of losses from the past or future operations. DoD sponsors may only assign tasks which take advantage of the core capabilities and unique characteristics of the FFRDC, as established in the sponsoring agreement. Additionally, Congress sets annual limits on the amount of staff-years of technical effort that may be funded for FFRDC s. Historically, funding placed on contract to the FFRDCs is less than one percent of the sponsor's budgetary resources. Together, the sponsoring agreements, contract terms, and Congressional controls on staff-years of effort and funding, serve to limit the Federal Government's exposure to financial and non-financial risks arising from FFRDC relationships.

RAND-NDRI funds were provided for Evaluating the Quality and Safety of Pain Care and Prescription Opioid Use in the MHS and for Evidence Synthesis of Sexual Assault and Sexual Harassment Topics to support FY 2019 *NDAA* Sec 702 Response.

James Lovell Federal Health Center

This health care facility located in North Chicago, Illinois is a joint venture between BUMED, and the VA established by *Section 1704 of P.L. 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.

Medicare-Eligible Retiree Health Care Fund

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

Note 20. Insurance Programs

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 Continued Health Care Benefits Program (CHCBP), TRICARE Young Adult (TYA), TRICARE Reserve Select (TRS), TRICARE Retired Reserve (TRR), TRICARE Prime Remote (TPR) and Select which together make up the TRICARE Insurance Portfolio. Most of these programs are intended to be budget neutral, meaning that the premiums should match the outlays, and are exchange transaction insurance programs. Premiums are adjusted either upward, or downward for each calendar 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 prior calendar years. Premiums are based on the Program's benefit cost, which eliminates any inherent risk to third parties, including the beneficiary and the MCSCs who provide health care claims processing and the initial collections on behalf of DHA-CRM. The total amount of Insurance Premium collections in FY 2021 was $864.9 million and $755.6 million for FY 2020. The benefit cost for FY 2021 correlate to the premium collections reported.

For Calendar Year (CY) 2021 Monthly Premium Rates are established on an annual basis in accordance with title *10 U.S.C. Sections 1076d, 1076e, 1078a, and 1110b* along with *title 32, Code of Federal Regulations, part 199.20, 24, 25 and 26*, as enacted by *Section 701 of NDAA* for FY 2017; P.L. 114 328. The enrollment fee and or premium collections are credited to DHP appropriation available for the FY 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. 1075 and 1075a. 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 TRICARE Encounter Data Set (TEDS). The liability balance represents unpaid claims received as of the end of the reporting period. The risk for future claim cost is 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 in 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 2021	FY 2020
Beginning Balance	$ 1,966,037	$ 2,038,491
Claims Expense	15,074,537	14,040,316
Claims Adjustment Expenses	(22,282)	(30,375)
Payments to Settle Claims	(14,918,922)	(14,098,748)
Recoveries and Other Adjustments	(14,692)	16,353
Ending Balance	$ 2,084,678	$ 1,966,037

Note 21. COVID-19 Activity

Coronavirus Aid, Relief and Economic Security Act

On March 27, 2020, the *CARES Act* was signed into law, which provides FY2020 supplemental appropriations for federal agencies to respond to COVID-19. The supplemental appropriations are designated as emergency spending, which is exempt from discretionary spending limits. DHP was appropriated approximately $3.8 billion to prevent, prepare for, and respond to COVID-19, including to provide additional funds to maintain normal operations and cover other necessary authorized activities domestically or internationally during the period that the programs are impacted by the COVID-19.

On April 10, 2020, the Office of Management and Budget (OMB) issued implementation guidance for supplemental funding provided in response to the COVID-19. In balancing speed with transparency, OMB Memorandum M-20-21 directed agencies to leverage and continue to employ existing financial transparency and accountability mechanisms wherever possible. OMB M-20-21 further instructed agencies to consider three core principles: (1) mission achievement, by using data and evidence to meet program objectives; (2) expediency in issuing awards to meet crucial needs; and (3) transparency and accountability to the public.

Funding Usage

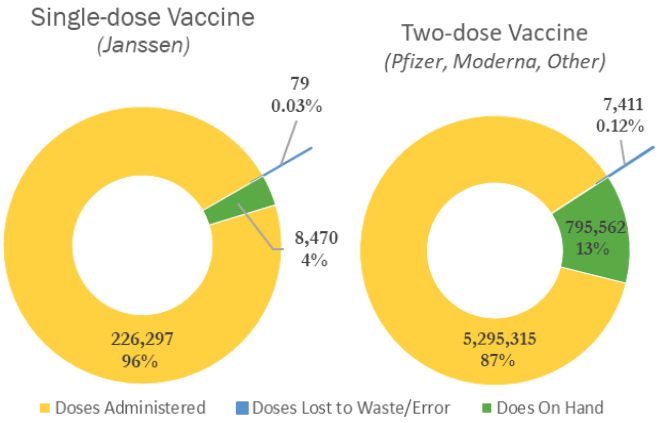
DHP distributes funding received from the *CARES Act* to its different components for usage. While funds were re-distributed amongst components in FY 2021, no additional *CARES Act* funds were received in FY 2021. See the table below for more details regarding distribution and usage of *CARES Act* funds by DHP component.

(dollars in thousands)	*Unaudited*					
DHP Component	FY 2021			FY 2020		
	Distributed	Obligated	Unobligated	Distributed	Obligated	Unobligated
MEDCOM	$ 28,840	$ (22,828)	$ 95,557	$ 463,811	$ 419,923	$ 43,888
BUMED	6,147	26,175	46,926	249,941	182,988	66,953
AFMS	28,412	16,931	15,309	152,349	148,521	3,828
DHA	(90,002)	180,811	40,920	1,415,253	1,103,519	311,734
Direct Care Financial Management (DCFM)	-	(5,054)	15,807	156,977	146,224	10,753
CRM	-	(116,292)	8,605	132,000	239,687	(107,687)
USUHS	26,603	4,436	5	14,481	36,643	(22,162)
Held at DHA	-	-	115	115	-	115
Total	**$ -**	**$ 84,178**	**$ 223,244**	**$ 2,584,927**	**$ 2,277,505**	**$ 307,422**

COVID-19 Vaccine Administration and Statistics

DHP entered into an agreement with the U.S. Department of Health and Human Services Center for Disease Control and Prevention (CDC) on November 20, 2020 to transfer on or more of the United States Government purchased COVID-19 vaccines, syringes, needles and other constituent products, and other ancillary supplies at no cost to DHP. As a result, DHP has not reported such items described as inventory within its financial statements or accompanying footnotes. The agreement between DHP and the CDC outlines appropriate vaccine distribution, management, and monitoring of DHP's plans for COVID-19 vaccination. DHP agreed to Administer COVID-19 Vaccines in accordance with all requirements and recommendations of CDC and CDC's Advisory Committee on Immunization Practices.

During FY 2021, DHP administered over 5 million doses of the Pfizer, Moderna, and Janssen COVID-19 vaccines. See the charts below for a summarization of DHP's COVID-19 vaccine efforts in FY 2021.



Other Information

As of September 30, 2021, total FY 2021 obligations related to the funding received for COVID-19 were approximately $84 million and approximately $223 million remains unobligated.

The impact on the entity's assets, liabilities, costs, revenues, and net position cannot yet be determined. The following footnotes also contain disclosures related to COVID-19 activities:

- Note 3: Fund Balance with Treasury
- Note 5: Accounts Receivable, Net
- Note 12: Other Liabilities

Note 22. Subsequent Events

Subsequent events after the balance sheet date have been evaluated through the auditors' report date. Management determined that there are no additional items to disclose.

Required Supplementary Information

This section provides the deferred maintenance and repairs (DM&R) disclosures, required in accordance with SFFAS 42, *Deferred Maintenance and Repairs: Amending Statements of Federal Financial Accounting Standards 6, 14, 29, and 32*, and the Combined Statement of Budgetary Resources. Maintenance and repairs for real property assets that were not performed when they should have been or were scheduled and delayed for a future period are considered DM&R.

Deferred Maintenance and Repairs

DHP tracks and report deferred maintenance and repair of its PP&E in accordance with *SFFAS 42*. DM&R relate solely to capitalized general PP&E and stewardship PP&E.

DM&R are maintenance and repairs that were not performed when they should have been or were scheduled to be and which are put off or delayed for a future period.

Maintenance and repairs are activities directed toward keeping fixed assets in an acceptable condition. Activities include preventive maintenance; replacement of parts, systems, or components; and other activities needed to preserve or maintain the asset. Maintenance and repairs, as distinguished from capital improvements, exclude activities directed towards expanding the capacity of an asset or otherwise upgrading it to serve needs different from, or significantly greater than, its current use.

DHP Deferred Maintenance consisted of the following as of September 30, 2021 and 2020 *(dollars in thousands):*

	Unaudited FY 2021		
Property Type	Plant Replacement Value	Required Work (Deferred Maintenance & Repair)	Percentage
Category 1	$ 40,795	$ 3,903	10%
Category 2 (Excluded)	$ -	$ -	-
Category 3	$ 3,101	$ 403	13%
Total	**$ 43,896**	**$ 4,306**	**10%**

	Unaudited FY 2020		
Property Type	Plant Replacement Value	Required Work (Deferred Maintenance & Repair)	Percentage
Category 1	$ 32,420	$ 2,796	9%
Category 2 (Excluded)	$ -	$ -	-
Category 3	$ 2,397	$ 250	10%
Total	**$ 34,817**	**$ 3,046**	**9%**

*NOTE: The DHA Real Property Team provides BUILDER with Inventory updates annually in October. FY20 balance is lower due to a major BUILDER data cleanup mostly on AF assets in earlier this year.

All DHP assets are not currently in BUILDER due to inventory discrepancies resulting from on-going negotiations with the services regarding readiness facilities and on-going DHA Real Property reconciliation efforts with the Military Departments.

DHP Funded assets are continuously being added and removed from the inventory due to on-going mission changes.

DHA Real Property Team continues to work with the Military Departments in their Accountable Property System of Record (APSR).

Facility Categories defined:

- **Category 1:** Buildings, Structures, and Linear Structures that are enduring and required to support an ongoing mission,
- **Category 2:** Buildings, Structures, and Linear Structures (Excess Facilities or Planned for Replacement)
- **Category 3:** Buildings, Structures, and Liner Structures that are Heritage assets (historical, cultural, or architectural)

To facilitate DM&R reporting, the Department of Defense mandated the use of the BUILDER™ program for all Condition and Facility Condition Index (FCI) reporting effective 10 Sep 13. The Assistant Secretary of Defense – Health Affairs, directed the implementation of the BUILDER program in a memo dated 10 Jan 2014 and charged the DHA Facility Director with the responsibility of completing the Implementation. FCI is the primary metric used by DHP to measure/score the condition of real property and is calculated as shown in *Figure 25* below.

Figure 25: Shows how the FCI is calculated.

$$FCI = \left(1 - \frac{\sum Deferred\ Maintenance\ and\ Repair\ (DM\&R)}{\sum Plant\ Replacement\ Value\ (PRV)}\right) * 100$$

The FCI formula numerators makes up the total deferred Real Property Maintenance & Repair while the addition of a multiplication of 100 creates a scoring of 100 (good) to 0 (bad) ranking system without decimals for easy identification of building's conditions.

Maintenance and Repair Policies

The DHA operates over 1,900 (facilities) throughout the world and includes 88 historical buildings. Most of the facilities are predominantly used to support the MHS mission for healthcare delivery. DHA's policy ensures patient safety and world class healthcare for all our beneficiaries.

	Count	Historical	Non-Historical	Note:
DHP Structures	1,675	88	1,587	Unit of Measure = Square Feet
DHP Non-Structure Support Assets	261	0	261	Unit(s)of Measure = Tons, Gallons, Kilovolts, etc.
Totals	1,936	88	1,848	

As permitted under *SFFAS 42*, the DHA employs a parametric estimating method from BUILDER for the largest portion of its portfolio (Health Care facilities). Health care facilities are being reviewed continually through the BUILDER Annual Work Plan. DHA assets in BUILDER are monitored annually as part of the Work Item remediation process. Any Work Items not remediated when identified by BUILDER become the basis DM&R. DHA plans to continue to add to the BUILDER inventory as more real property assets is reconciled with the Military Departments.

Uniformat is a standard for classifying building specifications, cost estimating and cost analysis in the US and Canada which adheres to the American Society for Testing and Materials (ASTM) 1557 Building Standards and developed by the General Service Administration (GSA) and the American Institute of Architects (AIA) in 1972. Uniformat types are common to all facilities regardless of real property categories and *Figure 26* below provides clarification.

Figure 26: Uniformat types.

UNIFORMAT Type	Included in DMR Calculation	Excluded in DMR Calculation
A10 FOUNDATIONS		X
A20 BASEMENT CONSTRUCTION		X
B10 SUPERSTRUCTURE		X
B20 EXTERIOR ENCLOSURE	X	
B30 ROOFING	X	
C10 INTERIOR CONSTRUCTION	X	
C20 STAIRS		X
C30 INTERIOR FINISHES	X	
D10 CONVEYING	X	
D20 PLUMBING	X	
D30 HVAC	X	
D40 FIRE PROTECTION	X	
D50 ELECTRICAL	X	
E10 EQUIPMENT	X	
E20 FURNISHINGS	X	
F10 SPECIAL CONSTRUCTION	X	
G20 SITE IMPROVMENTS	X	
G30 SITE CIVIL/MECHANICAL UTILITIES	X	
G40 SITE ELECTRICAL UTILITIES		X
G90 OTHER SITE CONSTRUCTION		X

BUILDER is a predictive modeling tool, but not the sole decision-making tool for making DM&R decisions. Mission, budget constraints, emerging threats, operational issues, and a host of other consideration go into making the decision on where funding is spent. The BUILDER Program was chosen by the DOD because its condition standards, related assessment methods, and reporting formats are consistently applied across the DOD inventory. BUILDER uses Standards and Policies (S&P) to predict and then track Work Items (Sections / Equipment) that are nearing or have passed the end of their useful life. Please Refer to Interim Procedures Memorandum 19-005, BUILDER™ Sustainment Management System (SMS) June 18, 2019, Para. 3.e-j for a full description of S&P development, AWP development, and AWI remediation.

The current "Standard" is measured by Remaining Service Life (RSL), that assumes, all sustainment activities have occurred during the equipment's life and that the equipment hasn't failed early, that the reliability of the equipment is diminished enough that the equipment should be replaced (Restored).

Maintenance and Repair Prioritization and Acceptable Condition Standards

DHP's current prioritization policy is based on the number of years of RSL and categorized by equipment type (a.k.a. System or UNIFORMAT).

UNIFORMATS with long service lives do not trigger replacement Work Items until they are very near the end of their useful life – 2 years. As an example, Foundations have a useful life of between 70 & 120 years and so applying the Policy would not generate a replacement Work Item until the Foundation was 68 or 118 years old.

UNIFORMATS with shorter Service Lives, but that carry a greater risk should the equipment fail, generate a Replacement Work Item 3 years before the end of their useful life. This would include super structures such as doors and windows.

UNIFORMATS with shorter Service Lives, but that carry a severe risk should the equipment fail, generate a Replacement Work Item 4 years before the end of their useful life. This would include a cross-section of UNIFORMATs types such as Fire Protection Systems, Boilers and Chillers, and Roofs.

The primary factors that BUILDER considers in determining acceptable condition standards are Equipment Service life, RSL, and risk of that equipment's failure to the Facilities performance. Healthcare facility medical centers and some of their support facilities (Central Utility or Electric Plants) have a zero-failure risk – there is no allowance for failure, the equipment must work immediately upon demand (e.g., back-up generators must come online and perform at 100% of their rated output within 10 seconds of demand).

Deferred Maintenance and Repair Exclusions

Category 1 & 3 assets are included in DM&R calculations.

Category 2 assets are not included in DM&R calculations as they are appropriated through the MILCON funding program and being new, have no associated DM&R.

Category 1 & 3 assets are further broken down by building UNIFORMATs, with Included and Excluded UNIFORMAT Types.

Included UNIFORMAT Rationale

Equipment (Infra-structure) of these UNIFORMAT types will be replaced regularly during the lifecycle of the Structure (Asset) ICW BUILDER's projected lifecycle. These UNIFORMATS are capitalized over the life of the Individual Equipment.

Excluded UNIFORMAT Rationale

Although these infra-structure types may be repaired if necessary, throughout the life of an asset, there is no programed replacement for these UNIFORMAT types. These UNIFORMATS are capitalized over the life of the Structure / Asset.

Individual DMR Work Item Cost Threshold.

Market research and DHA work processes support the use of a $10,000 or greater cost as the reporting threshold for DMR work items.

Significant Changes in Deferred Maintenance and Repair

With the FY 20/21 roll-over, significant data update activities occurred that will affect DMR Calculations:

Plant Replacement Values (PRV). Plant Replacement Values had not been updated in the BUILDER Database since April of 2019. As part of the FY rollover, all PRVs were updated to reflect their corresponding DMLSS-FM PRVs. As would be expected the individual Asset PRVs varied, but in the aggregate PRVs increased.

Note: The SMS BUILDER Cost book is currently under revision by CERL to incorporate R.S. Means Cost Works data and we anticipate that this will lead to substantially increased Work Item Costs, and therefore an increase in DMR backlog. FE intends to wait until CERL's updates are completed before beginning to use the new R.S. Means costs and will decide after analyzing the new costs.

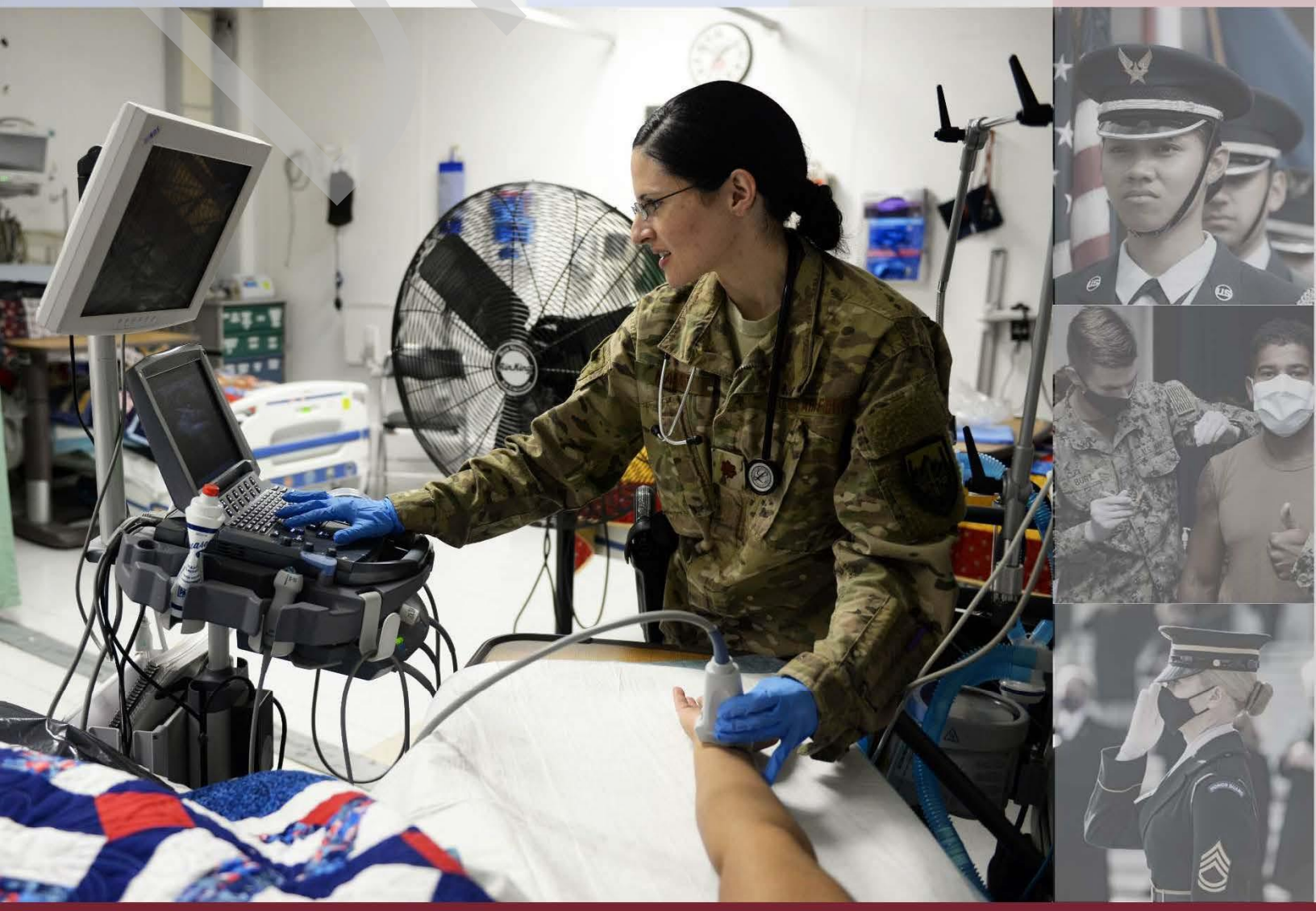
Combining Statement of Budgetary Resources

As of September 30, 2021 (dollars in thousands):

	Unaudited				
	Operations, Readiness & Support	Procurement	Research, Development, Test & Evaluation	Family Housing and Military Construction	Combined Totals
Budgetary Resources					
Unobligated Balance from Prior Year Budget Authority, net (discretionary and mandatory)	$ 2,278,152	$ 387,399	$ 2,698,616	$ 638,705	$ 6,002,872
Appropriations (discretionary and mandatory)	31,614,930	452,455	2,395,079	383,778	34,846,242
Contract Authority (discretionary and mandatory)	-	-	-	-	-
Spending Authority from Offsetting Collections (discretionary and mandatory)	4,175,347	4,029	3,359	-	4,182,735
Total Budgetary Resources	**$ 38,068,429**	**$ 843,883**	**$ 5,097,054**	**$ 1,022,483**	**$ 45,031,849**
Status of Budgetary Resources					
New Obligations and Upward Adjustments (total)	$ 36,782,810	$ 541,400	$ 3,150,768	$ 574,911	$ 41,049,889
Unobligated Balance, end of year:					
Apportioned, Unexpired Accounts	69,960	280,499	1,837,966	386,257	2,574,682
Exempt from apportionment, unexpired Accounts	128	-	-	-	128
Unapportioned, Unexpired Accounts	-	-	-	-	-
Unexpired Unobligated Balance	70,088	280,499	1,837,966	386,257	2,574,810
Expired Unobligated Balance	1,215,531	21,984	108,320	61,315	1,407,150
Unobligated Balance, end of year (total)	1,285,619	302,483	1,946,286	447,572	3,981,960
Total Budgetary Resources	**$ 38,068,429**	**$ 843,883**	**$ 5,097,054**	**$ 1,022,483**	**$ 45,031,849**
Outlays, net					
Outlays, net (total) (discretionary and mandatory)	$ 32,120,101	$ 454,908	$ 2,336,560	$ 546,167	$ 35,457,736
Distributed Offsetting Receipts	-	-	-	-	-
Agency Outlays, net (discretionary and mandatory)	**$ 32,120,101**	**$ 454,908**	**$ 2,336,560**	**$ 546,167**	**$ 35,457,736**

As of September 30, 2020 (dollars in thousands):

	Operations, Readiness & Support	Procurement	*Unaudited* Research, Development, Test & Evaluation	Family Housing and Military Construction	Combined Totals
Budgetary Resources					
Unobligated Balance from Prior Year Budget Authority, net (discretionary and mandatory)	$ 2,188,951	$ 319,599	$ 1,655,074	$ 779,966	$ 4,943,590
Appropriations (discretionary and mandatory)	33,515,934	623,762	3,677,187	337,790	38,154,673
Contract Authority (discretionary and mandatory)	-	-	-	-	-
Spending Authority from Offsetting Collections (discretionary and mandatory)	3,951,352	29,462	(27,214)	-	3,953,600
Total Budgetary Resources	**$ 39,656,237**	**$ 972,822**	**$ 5,305,048**	**$ 1,117,756**	**$ 47,051,863**
Status of Budgetary Resources					
New Obligations and Upward Adjustments (total)	$ 37,980,857	$ 632,421	$ 2,833,685	$ 500,475	$ 41,947,438
Unobligated Balance, end of year:					
Apportioned, Unexpired Accounts	748,621	300,910	2,357,198	542,131	3,948,860
Exempt from apportionment, unexpired Accounts	36	-	-	-	36
Unapportioned, Unexpired Accounts	-	60	-	-	60
Unexpired Unobligated Balance	748,657	300,970	2,357,198	542,131	3,948,956
Expired Unobligated Balance	926,723	39,431	114,166	75,150	1,155,470
Unobligated Balance, end of year (total)	1,675,380	340,401	2,471,363	617,282	5,104,426
Total Budgetary Resources	**$ 39,656,237**	**$ 972,822**	**$ 5,305,048**	**$ 1,117,757**	**$ 47,051,864**
Outlays, Net					
Outlays, net (total) (discretionary and mandatory)	$ 31,954,104	$ 354,338	$ 1,784,965	$ 526,402	$ 34,619,809
Distributed Offsetting Receipts	-	-	3,129	-	3,129
Agency Outlays, net (discretionary and mandatory)	**$ 31,954,104**	**$ 354,338**	**$ 1,788,094**	**$ 526,402**	**$ 34,622,938**



Other Information

Section III

Summary of Financial Statement Audit and Management Assurances

Table below provides a summary of financial statement audit.[3]

Summary of Financial Statement Audit					
Audit Opinion	Disclaimer				
Restatement	No				
Material Weaknesses	**Beginning Balance**	**New**	**Resolved**	**Consolidated**	**Ending Balance**
Accounting and Financial Reporting Governance Structure, Entity-Level Controls	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**
Stockpile Materials	1	-	-	-	**1**
Liabilities and Related Expenses	1	-	-	-	**1**
Monitoring and Reporting of Obligations and Adjustments	1	-	-	-	**1**
Information System	1	-	-	-	**1**
Total Material Weaknesses	11	-	-	-	11

[3] The summary of financial statement audit of material weaknesses is from the Independent Auditor's (IPA) DHP Report on ICOFR. Per OMB Circular A-136 significant deficiencies are not required to be disclosed.

Table below provides a summary of management assurances[4]

Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)						
Statement of Assurance	No Assurance					
Material Weaknesses *(Assessable Unit)*	**Beginning Balance**	**Reclassified**	**New**	**Resolved**	**Consolidated**	**Ending Balance**
Financial Reporting – Compilation	2	-2	-	-	-	-
Financial Reporting – Universe of Transaction Reconciliations	2	-2	-	-	-	-
Medical Revenue and Associated Receivables	1	-1	-	-	-	-
General Equipment Existence and Completeness	1	-1	-	-	-	-
Valuation of Property, Plant, and Equipment	2	-2	-	-	-	-
Accounts Receivable	-	-	1	-	-	1
Financial Reporting	-	-	5	-1	-	4
Equipment Assets	-	-	1	-	-	1
Real Property Assets	-	-	1	-	-	1
Internal Use Software (IUS)	-	-	1	-	-	1
Total Material Weaknesses	8	-8	9	-1	-	8

Effectiveness of Internal Control over Operations (FMFIA § 2)						
Statement of Assurance	No Assurance					
Material Weaknesses *(Assessable Unit)*	**Beginning Balance**	**Reclassified**	**New**	**Resolved**	**Consolidated**	**Ending Balance**
Fund Balance with Treasury	1	-1	-	-	-	-
General Equipment	1	-1	-	-	-	-
Governance Structure and Entity-Level Controls	10	-10	-	-	-	-
Information Systems	5	-5	-	-	-	-
Liabilities	2	-2	-	-	-	-
Acquisition	-	-	6	-	-	6
Comptroller and Resource Management	-	-	4	-	-	4
Communications	-	-	2	-1	-	1
Contract Administration	-	-	6	-1	-	5
Information Technology – Business System Modernization	-	-	3	-	-	3
Personnel and Organizational Management	-	-	8	-	-	8
Total Material Weaknesses	19	-19	29	-2	-	27

[4] The total number of material weaknesses and non-Compliances for ICOFR, ICO and internal controls over federal financial management system requirements are self-identified by DHP Management and exclude material weaknesses identified by IPA per the OSD's *Fiscal Year 2020 Department of Defense Statement of Assurance Execution Handbook*. As referenced in Management's Response to the Independent Auditor's Report, Management agrees with the auditor identified material weaknesses. Also, Per OMB Circular A-136 significant deficiencies are not required to be disclosed.

Conformance with Federal Financial Management System Requirements (FMFIA§ 4)						
Statement of Assurance	No Assurance					
Material Weaknesses *(Assessable Unit)*	**Beginning Balance**	**Reclassified**	**New**	**Resolved**	**Consolidated**	**Ending Balance**
Access Controls	-	-	1	-	-	**1**
Continuity Planning	-	-	1	-	-	**1**
Data Management Controls	-	-	1	-	-	**1**
Total Material Weaknesses	-	-	3	-	-	3

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

Management's assessment of FFMIA compliance was completed prior to the results of the FY 2021 financial statement audit. Our auditor has noted 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 Reporting over Financial Reporting. DHP is in the process of evaluating the FY 2021 audit findings contributing to noncompliance to continue the process of formulating and implementing remediation plans necessary to bring the financial managements systems into substantial compliance.

Management Challenges

Global Pandemics and Extreme Weather Events

In the DoD Office of the Inspector General's (DoD OIG) *FY 2021 Top DoD Management Challenges* report, the DoD OIG identified non-traditional threats, such as pandemics and extreme weather events, to their list of challenges, in addition to those identified in previous years. Both pandemics and extreme weather events require that DoD develop long-term strategies to reduce vulnerabilities to personnel readiness and infrastructure. During the pandemic, the DoD was confronted with the task of maintaining unit and individual readiness, while simultaneously assisting other Federal agencies with their responses to COVID-19 and other events. Dependence on the MHS to respond to non-traditional threats requires heightened and concerted investment in the refinement or development of policies and procedures to enable rapid response to public health emergencies. Although the MHS responded well to the pandemic, lessons learned were documented and are being addressed to hone our readiness for future events and bolster the resiliency of our medical enterprise.

Ensuring Health and Safety of Military Personnel, Retirees, and Their Families

Per the DoD IG report, the MHS has experienced several challenges with maintaining adequate access to high-quality healthcare as we implement statutory MHS reform. The objective of these reforms is to standardize business and clinical processes, eliminate silos of military health, improve medical readiness, and maintain quality and accessible healthcare for the 9.6 million eligible MHS beneficiaries. The DHA has implemented a phased approach to transition DoD MTFs to DHA's administration and management, relying on support from the Military Departments to administer the MTFs while DHA establishes local market offices to support the transition. The OASD(HA) and DHA are developing and publishing policies and procedures to standardize business practices across the MHS enterprise to gain efficiencies while facilitating the transition.

Deployment and Interoperability of Electronic Health Records

As stated in the DoD IG report, the DoD deployed a new electronic health records (EHR) system, MHS GENESIS, in 2017 to help ensure seamless care throughout the life of military members and beneficiaries. MHS GENESIS is being jointly developed and operated with the Department of Veterans Affairs (VA) and is intended to standardize the management and delivery of healthcare for the DoD's 9.6 million beneficiaries and the 9.1 million beneficiaries supported by the VA. MHS GENESIS should provide enhanced, secure technology to access and manage patient health. The DoD continues to deploy MHS GENESIS while addressing implementation issues and known system shortfalls. Recent feedback from MTFs has been positive. The DHA aims to field MHS GENESIS to all MTFs by 2024.

Suicide Prevention

Suicide prevention continues to be a top priority for DoD and Congress. DoD leadership continues to develop strategies and employ efforts at all echelons to raise awareness of and prevent suicide. The Vice Chairman of the Joint Chiefs of Staff said in September 2020, "Regardless of the uniform we wear, we are not immune from life's challenges, including thoughts of suicide," and also stressed, "Ending suicide in our ranks is a top priority." The Department's suicide prevention efforts are guided by the 2015 Defense Strategy for Suicide Prevention. This strategy created the foundation for our prevention activities by using a public health approach, which acknowledges a complex interplay of individual-, relationship-, and community-level risk factors. The DoD has several efforts underway to support Service members and their families, including those aimed at increasing access to support, reducing barriers to receiving support, and targeting our populations of greatest concern.

Impact of Environmental Hazards on DoD Personnel

Environmental hazards such as lead-based paint, asbestos-containing material, and contaminated drinking water continue to be well-known threats to military personnel and their families. Emerging contaminants and pollutants that are not regulated or are loosely regulated pose challenges for DoD as officials work to mitigate potential risks. Emerging contaminants include perfluoroalkyl and polyfluoroalkyl substances (PFAS), also known as "forever chemicals," which are found in everyday consumer items, from nonstick cookware to water-resistant clothing. The DoD and the U.S. Environmental Protection Agency have been participating in studies and taking actions to characterize, identify, and develop methods to test for and dispose of PFAS since the early 2000s, and in 2019 DoD established the DoD PFAS Task Force. Another environmental concern the DoD is addressing is the effects of open-air burn pits which were commonly used in Iraq and Afghanistan to dispose of a variety of waste products. The DoD is collaborating with the VA to identify Service members exposed to the burn pits so that long-term health effects can be tracked. DoD issued

guidance in 2017 to establish procedures for assessing significant long-term health risks from past environmental exposures while living or working on military installations.

Conclusion

A rapid, organized response to non-traditional threats such as pandemics and extreme weather events demands training and the development of cohesive policies and procedures to ensure that we have both medically ready forces, and a ready medical force. While the MHS participates in the "whole of government" emergency response pandemic and extreme weather training exercises, increased familiarity with roles and responsibilities is needed. As we continue to reform the MHS, we will continue to weigh the risks to force readiness and the health of our beneficiaries. We will continue to address concerns with the deployment of MHS GENESIS and work to implement fixes and to ensure interoperability with the VA. While patient visits to outpatient mental health and substance abuse programs have increased, efforts to stem substance abuse and suicide are ongoing and will continue to be DoD priorities. The MHS is committed to providing service members, retirees, and their families with access to high-quality healthcare and to collaborating with the VA to ensure a seamless continuation of access once members transition out of the military.

Payment Integrity Information Act Reporting

In accordance with the *Payment Integrity Information Act of 2019* (P. L. 116-117, 31 U.S.C § 3352 and § 3357) and Appendix B of the OMB Bulletin No. 21-04, *Audit Requirements for Federal Financial Statements*, dated June 11, 2021, DoD reports payment integrity information (i.e., improper payments) at the agency-wide 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/afr2021.aspx*.

Fraud Reduction Report

As a healthcare organization, the MHS is just as susceptible to healthcare fraud schemes as any other medical organization. Several federal laws governing fraud and abuse exist that specify the criminal, civil, and administrative penalties and remedies the government may impose on individuals or entities that commit fraud and abuse federal programs such as TRICARE. Violating these laws may result in nonpayment of claims, Civil Monetary Penalties, exclusion from all Federal healthcare programs, and criminal and civil liability. Government agencies, including the U.S. Department of Justice (DOJ), HHS, the HHS Office of Inspector General (OIG), and the Centers for Medicare and Medicaid Services (CMS), enforce these laws.

Within DoD and pursuant to *DoD Directive 5106.01*, the DoD Inspector General (DoD IG) serves as the principal advisor to the Secretary of Defense on all audit and criminal investigative matters and for matters relating to the prevention and detection of fraud, waste, and abuse in the programs and operations of the DoD. The DoD IG initiates, conducts, supervises, and coordinates such audits, investigations, evaluations, and inspections within the DoD, including the Military Departments, as the IG DoD considers appropriate. In addition, the DoD IG provides policy and direction for audits, investigations, evaluations, and inspections relating to fraud, waste, abuse, program effectiveness, and other relevant areas within DoD IG responsibilities.

In accordance with *DoD Instruction 7050.01*, it is DoD policy that:

a) Preventing and detecting fraud, waste, abuse, and mismanagement in DoD programs and operations promotes efficiency, economy, and effectiveness.

b) DoD personnel are required to report suspected fraud, waste, abuse, mismanagement, and other matters of concern to DoD without fear of reprisal.

c) The OIG DoD maintains the DoD Hotline Program.

The MHS relies on the services of the DoD IG and its Defense Criminal Investigative Service (DCIS) in our efforts to identify and deter fraud, waste, and abuse. The mission of DCIS is to conduct criminal investigations of matters related to DoD programs and operations, focusing on procurement fraud, public corruption, product substitution, health care fraud, illegal technology transfer, and cyber-crimes and computer intrusions. DCIS has the legal authority to investigate military personnel, government and non-government civilians, foreign citizens, and U.S. and foreign companies alleged to have defrauded the DoD or criminally impacted DoD programs or operations. DCIS partners with federal, state, local and tribal law enforcement as needed, and frequently work with the Federal Bureau of Investigations, Homeland Security Investigations, Army Criminal Investigations Command, Naval Criminal Investigative Service, and Air Force Office of Special Investigations. Other Office of Inspector General partners include Veterans Affairs, HHS, and DoJ.

The DHA Program Integrity Office in Aurora, Colorado is responsible for healthcare anti-fraud to safeguard beneficiaries and protect benefit dollars. DHA PI develops and executes anti-fraud and abuse policies and procedures, provides oversight of contractor program integrity activities, and coordinates investigative activities. DHA PI also develops cases for criminal prosecutions, civil litigations, and initiates administrative measures. Through a Memorandum of Understanding (MOU), DHA PI refers its fraud cases to the Defense Criminal Investigative Services. DHA PI also coordinates investigative activities with Military Criminal Investigative Offices, as well as other federal, state, and local agencies.

Figure 27: Program integrity recoveries/cost avoidance (source: FY 2021 *Evaluation of the TRICARE Program* Report).

PROGRAM INTEGRITY RECOVERIES/COST AVOIDANCE ($ MILLIONS), CYs 2017–2019

	CY 2017	CY 2018	CY 2019
Total Recoveries	$88.8	$149.4	$363.6
Court-Ordered Fraud Judgments/Settlements	$66.3	$125.9	$328.2
PI Contractor Administrative Recoupment/Offsets (Received)	$22.5	$23.5	$34.4
Total PI Contractors Cost Avoidance	$55.0	$48.9	$67.5
Contractor Prepayment Reviews	$53.6	$48.5	$67.5
Excluded Providers	$1.4	$0.4	$0.1

Sources: 2019 Annual Program Integrity Operational Report/Contractor Submitted Fraud and Abuse Reports, CY 2017–CY 2019; CY 2019 data are the latest reported as of 9/24/2020.

Program Savings and Claim Recoveries – New reimbursement approaches are continually evaluated for potential savings to TRICARE as summarized in *Figure 27* for calendar years 2017-2019. As new programs are established, savings are estimated and

monitored. Claim recoveries result from identified overpayments adjusted in TRICARE Encounter Data (TED), and the differences are recouped.

- **Recovery A** – Post-payment Duplicate Claim Recoveries: A post-payment duplicate claims system was developed by DHA as a retrospective auditing tool. It facilitates the identification of actual duplicate claim payments and the initiation and tracking of recoupments. *Figure 28* below provides the historical recovery of duplicate claims payments.

Figure 28: Summary of recoveries (source: FY 2021 *Evaluation of the TRICARE Program* Report).

RECOVERIES ($ MILLIONS), FYs 2018–2020

RECOVERIES	FY 2018	FY 2019	FY 2020
Post-Payment Duplicate Claim Recoveries	$4.5	$20.2	$21.1

- **Recovery B** – Improper Payment Recoveries: The DHA is vigilant in ensuring the accuracy of healthcare claims payments within the military health benefits program. The DHA has contracted with an external independent contractor (EIC) who is responsible for conducting post-payment accuracy reviews of TRICARE health benefit claims. The EIC is responsible for identifying improper payments made by TRICARE purchased care contractors as a result of contractor noncompliance with TRICARE policy, benefits, and/or reimbursement requirements.

Figure 29: Overpayments recaptured outside of payment recapture audits (source: FY 2021 *Evaluation of the TRICARE Program* Report).

OVERPAYMENTS RECAPTURED OUTSIDE OF PAYMENT RECAPTURE AUDITS ($ MILLIONS), FY 2020

ACTUAL OVERPAYMENT DOLLARS IDENTIFIED VIA RANDOM SAMPLES[a]	AMOUNT RECAPTURED (REFUNDS THROUGH FY 2020)
$13.85	$295.86

Sources: DHA/R&M (J-1/J-8)/Trust Fund and Revenue Cycle Management Improper Payment Evaluation Branch, 10/23/2020; Operational Reports and Quarterly Fraud and Abuse Reports

[a] "Actual overpayment dollars identified via random samples" in FY 2018 represents the total overpayment dollars from sampled claims.

Notes:

– DHA modified the methodology to calculate recoveries for this AFR (FY 2020). The methodology used in prior years could have overcounted refunds that were subsequently repaid. The modified methodology takes into consideration subsequent repayments and nets them against refunds, which lowered overall refunds.

– These numbers include recoupments for overpayments identified in audits as well as refunds occurring in the course of routine claim adjustments (for claims initially paid in FY 2018 and other fiscal years). DHA has no way to distinguish overpayment recoupments from routine claim adjustments.

– The Active Duty Dental Program (ADDP) refunds were calculated differently. The amount recovered in FY 2018 figure for ADDP represents refunds shown on contractor invoices to DHA. ADDP data is not included in the TED system, thus contractor invoices were used because TED transactions are not available.

In addition to the EIC post-payment reviews, DHA requires TRICARE purchased care contractors to use industry best practices when processing TRICARE claims. Contractors are required to use claims auditing software and develop prepayment initiatives that are manual and/or automated to avoid or prevent improper payments. *Figure 29* above provides FY 2020 improper payment recoveries of healthcare as a result of the EIC compliance reviews and ongoing purchased care contractor efforts to identify and recover improper payments.

The DHA Office of the Inspector General (DHA OIG) maintains a DHA Hotline Program, which includes inquiries addressing DHP. The hotline ensures inquiries resulting from allegations are conducted in accordance with applicable laws and DoD regulations and policies. The DHA 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, including those involving DHP.

The term "improper payment" are payments made by the government to the wrong person, in the wrong amount, or for the wrong reason. Although not all improper payments are fraud, and not all improper payments represent a loss to the government, all improper payments degrade the integrity of government programs and compromise citizens' trust in government. The definition is found in the *Payment Integrity Information Act of 2019* (P.L. 116-117) and the *OMB Circular A-123, Appendix C* (OMB M-18-20).

Under the direction of the OMB, agencies have identified the programs that are susceptible to significant improper payments, and measured, or are putting in place measurement plans, to determine the estimated number of improper payments. By identifying and measuring the problem, and determining the root causes of error, the government is able to focus its resources so that corrective action plans can be thoughtfully developed and successfully carried out.

The *Payment Integrity Information Act of 2019* and *OMB Circular A-123, Appendix C*, require Federal agencies to report information related to improper payments. The Payment Integrity Scorecard for military health benefits is available at www.paymentaccuracy.gov and reflected below in *Figure 30*.

Figure 30: Military Health Benefits Payment Integrity Scorecard.

Payment Integrity Scorecard

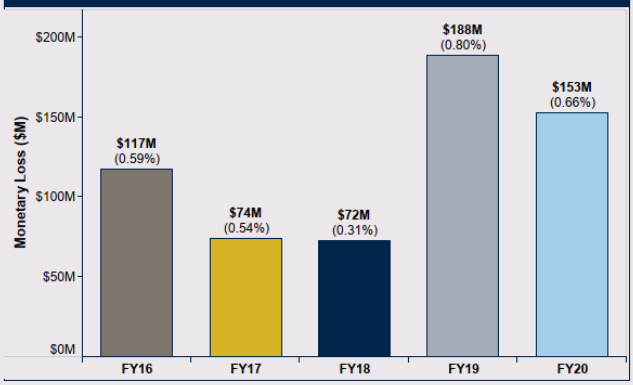
Program or Activity	Reporting Period
Military Health Benefits	Q3 2021

Change from Previous FY ($M) -$36M

DOD
Military Health Benefits

Brief Program Description:
Payments disbursed by the Defense Health Agency to private sector contractors for delivery of health care services to TRICARE eligible beneficiaries.

Monetary Loss ($M) (Overpayment as Percentage of Total Outlays)



	Key Milestones	Status	ECD
1	Develop mitigation strategies to get the payment right the first time	Completed	Jun-20
2	Evaluate the ROI of the mitigation strategy	Completed	Jun-20
3	Determine which strategies have the best ROI to prevent cash loss	Completed	Jun-20
4	Implement new mitigation strategies to prevent cash loss	Completed	Jun-20
5	Analyze results of implementing new strategies	Completed	Jun-20
6	Achieved compliance with PIIA	On-Track	May-22
7	Identified any data needs for mitigation	Completed	Mar-21

	Goals towards Reducing Monetary Loss		Status	ECD
1	Q3 2021	Perform quarterly reviews of all Contractors by monitoring and assessing healthcare claims processing performance.	On-Track	Jun-21
2	Q3 2021	Require TRICARE private sector contractors to perform assessments of their claims processing systems to determine programming errors and make necessary system modifications.	On-Track	Jun-21

	Recovery Method	Brief Description of Plans to Recover Overpayments	Brief Description of Actions Taken to Recover Overpayments
1	Recovery Activity	Continue scheduled compliance reviews conducted by EIC. Payment errors are identified and refunds made to the Government through the submission of an adjusted TED record or by direct payment.	Post payment compliance reviews identify payment errors for the purpose of reporting improper payment estimates. Private sector care Contractors are notified of payment errors for correction and to assess processes and procedures.
2	Recovery Activity	Continued recoupments occurring in the course of routine healthcare claims processing and adjustments as identified. Non-underwritten healthcare claims greater than $600, if not collected or offset, are referred to the DHA General Counsel.	Recoupments/refunds occurring in the course of routine healthcare claims processing, healthcare claim adjustments or corrections as identified by civilian providers or TRICARE beneficiaries.
3	Recovery Activity	Annual Cost of Healthcare Audit requires regional Contractors to recoup unallowable costs. Costs are extrapolated estimated overpayments to providers. Both regions submitted claim documents for initial audit of OP3 occurring in July and August 2021.	Contractual requirement for TRICARE private sector regional Contractors to recoup unallowable costs.

	Accomplishments in Reducing Monetary Loss	Date
1	Due to actions taken by the Contractor, error rates progressively reduced below contractual standard for FY19 Q1, Q2, Q3, & Q4. FY20 Q1, Q2, & Q3 error rates were also below the contractual standard of 1.75% at 0.81%, 0.56%, & 0.51% respectively.	Jun-21
2	The Annual Cost of Healthcare Audits for OP3 of the managed care contracts are currently being conducted by Concept Plus.	Jul-21
3	TRICARE private sector regional Contractor deployed Sprints 41-49, which delivered over 36 system updates to identified issues in claims processing.	Jul-21

Amt($)	Root Cause of Monetary Loss	Root Cause Description	Mitigation Strategy	Brief Description of Mitigation Strategy and Anticipated Impact
$143M	Administrative or process errors made by: others (participating lender, health care provider, or other organization administering Federal dollars)	TRICARE healthcare claim payments were incorrectly processed by Humana, one of our private sector contractors, which consisted of errors such as cost-share/deductible, duplicate payments, inaccurate invoices, and payments made to incorrect payee.	Mitigating strategy is to use mechanism in the contracts to recover erroneous payments.	Full recovery: Overpayments to providers and hospitals will be credited back to the government on future claims payments.

Monetary Loss - Monetary loss to the Government includes amounts that should not have been paid and in theory should/could be recovered.

Significant FY 2021 MHS Fraud Events (Source: DCIS)

March 23, 2021: Former children's autism service provider pays over $2.7 million to resolve healthcare fraud allegations

The former owner and sole shareholder of The Shape of Behavior (TSOB), a Texas-based provider of therapy services for children with autism, has agreed to pay to resolve allegations that the company submitted improper claims to the TRICARE program. Dr. Domonique Randall has now paid a total of $2,729,083.23. Authorities initiated an investigation after TRICARE's managed care support contractor -Humana Military Program Integrity -uncovered alleged improper claims. These were for applied behavior analysis therapy to beneficiaries with autism spectrum disorder. The settlement resolves allegations that nine separate TSOB locations submitted claims to TRICARE that misrepresented the identity of the actual rendering providers, that medical records could not substantiate or when individual providers billed excessive hours on individual dates of service. The Defense Health Agency -Office of Program Integrity, DCIS and Humana Military Program Integrity all assisted in the joint investigation resulting in the settlement.

March 22, 2021: Texas Doctor Accused of False Claims Act Violations

The United States Attorney's Office for the Northern District of Texas has filed a False Claims Act lawsuit against a Texas dermatopathologist and his clinic, Cockerell Dermatopathology (CDP), for submitting nearly $4.2 million in fraudulent claims to TRICARE. According to allegations in a civil complaint filed, Dr. Clay Cockerell, 64, knowingly permitted a laboratory management company to use his clinic's lab license to submit false claims to federal health insurance programs, including TRICARE, for medically unnecessary tests. The government is now seeking to recover millions in TRICARE payments that CDP previously admitted were improper, or, at a minimum, $3.485 million that CDP and Dr. Cockerell agreed they would pay to TRICARE.

March 18, 2021: Cardiologist Dinesh Shah Pays $2 Million To Resolve False Claims Act Allegations Relating to Excessive Testing

Dinesh M. Shah, M.D. and his practice, Michigan Physicians Group, P.C. (MPG) have paid the United States $2 million to resolve allegations that they violated the False Claims Act by knowingly billing federal healthcare programs for diagnostic testing that was either unnecessary or not performed. This settlement resolves allegations that from 2006 to 2017, Shah and MPG knowingly billed government programs, including Medicare, Medicaid, and TRICARE, for unnecessary diagnostic testing. This settlement comes after a years-long investigation by the Office of Inspector General for the United States Department of Health and Human Services and the Defense Health Agency acting on behalf of the TRICARE Program.

March 10, 2021: Chiropractor charged with falsely billing for procedure learned via YouTube

A Houston chiropractor and her medical group have been named in a civil suit under the False Claims Act alleging fraudulent billing, announced Acting U.S. Attorney Jennifer B. Lowery. Suhyun An owns and manages Campbell Medical Group PLLC and Johnson Medical Group PLLC dba Campbell Medical Clinic in the Spring Valley area of Houston. The civil complaint alleges An fraudulently obtained over $3.9 million from the Medicare and TRICARE programs by billing for the implantation of neurostimulator electrodes. These are surgical procedures usually requiring use of an operating room, and Medicare pays thousands of dollars for this procedure. The complaint alleges that neither An nor her clinic's employees performed surgery. Instead, they allegedly applied inexpensive devices used for electro-acupuncture. This procedure involves inserting needles into patients' ears with a neurostimulator taped behind the ears with an adhesive, according to the complaint. The lawsuit alleges nurse practitioners working for An learned how to apply the devices by watching YouTube videos and participating in trainings with sales representatives. The complaint alleges An knew the devices were not billable or recklessly disregarded that fact. The suit further claims she ignored emailed warnings from employees and outside billing companies including warnings that the devices were being labeled as "possible fraud."

February 10, 2021: Former Co-Owner of Pharmacy Pleads Guilty in Prescription Drug Billing Scheme

An additional defendant pleaded guilty in a long-running investigation into a prescription drug-billing scheme involving a Haleyville, Ala.-based pharmacy, Northside Pharmacy doing business as Global Compounding Pharmacy. This brings the total number of defendants who have pleaded guilty in the larger investigation to 26. According to the plea agreement, between August 2013 and June 2016, the defendant participated in a scheme to cause the pharmacy he worked at to bill for medically unnecessary prescription drugs. He participated in a scheme to direct employees to get medically unnecessary drugs for themselves, family members, and friends, to alter prescriptions to add non-prescribed drugs, to automatically refill prescriptions regardless of patient need, to routinely waive and discount co-pays to induce patients to obtain and retain medically unnecessary drugs, and to bill for drugs without patients' knowledge. According to the plea agreement, when prescription drug administrators attempted to police this conduct, the defendants evaded and obstructed those efforts, including by providing false information in response to audits and diverting their billing through affiliated pharmacies. The scheme targeted multiple health insurance plans, including the pharmacy's Blue Cross Blue Shield of Alabama plan, as well as plans providing health insurance to the elderly, disabled, members of the military, and veterans-Medicare, TRICARE, and CHAMPVA, among others.

February 2, 2021: Clinton Pharmacist Sentenced to 10 Years in Federal Prison for Conspiracy to Commit Health Care Fraud

Marco Bisa Hawkins Moran, 45, of Clinton, Mississippi, was sentenced to 120 months in federal prison followed by 3 years of supervised release for conspiring to commit health care fraud. Moran was also ordered to pay a monetary judgment of $12,195,740, restitution in the amount of $22,096,697, and a $20,000 fine. Between 2014 and 2016, Moran, as co-owner of Medworx Compounding and Custom Care Pharmacy, participated in a scheme to defraud TRICARE and other health care benefit programs, including those that provided coverage to employees of the City of Jackson, Mississippi. In total, the pharmacies submitted $22,068,144 in fraudulent claims to TRICARE and other health care benefit programs. As part of the scheme, Moran, and his co-conspirators, among other things, adjusted prescription formulas to ensure the highest reimbursement, paid marketers and physicians kickbacks and bribes to obtain prescriptions for high yield compounded medications irrespective of whether they were medically necessary, and routinely waived or reduced the collection of copayments.

January 15, 2021: Compounding Pharmacy Mogul Sentenced for Multimillion-Dollar Health Care Fraud Scheme

A Mississippi businessman was sentenced for his role in a multimillion-dollar scheme to defraud TRICARE. Wade Ashley Walters, a co-owner of numerous compounding pharmacies and pharmaceutical distributors, was sentenced on his guilty plea to one count of conspiracy to commit health care fraud and one count of conspiracy to commit money laundering. Walters was ordered to serve a total of 18 years in prison and to pay $287,659,569 in restitution. Walters was further ordered to forfeit $56,565,963, representing the proceeds he personally derived from the fraud scheme. Between 2012 and 2016, Walters orchestrated a scheme to defraud TRICARE and other health care benefit programs by distributing compounded medications that were not medically necessary. As part of the scheme, Walters, and his coconspirators, among other things, adjusted prescription formulas to ensure the highest reimbursement without regard to efficacy; solicited recruiters to procure prescriptions for high margin compounded medications and paid those recruiters commissions based on the percentage of the reimbursements paid by pharmacy benefit managers and health care benefit programs, including commissions on claims reimbursed by TRICARE.

January 12, 2021: Couple Sentenced for Obtaining $1.7 Million in Military Health Care Kickback Scheme

Richard and Kimberly Homrighausen were sentenced on January 7, 2021 by United States District Judge Barry W. Ashe for conspiracy to pay and receive kickbacks related to compounded medications paid for by TRICARE. At their guilty pleas, the defendants admitted to paying kickbacks to TRICARE beneficiaries to induce them to obtain compounded medications, costing TRICARE a total of approximately $9 million. To conceal the kickbacks, the defendants created a purported non-profit that paid off the beneficiaries under the guise of "grants" to thank them for their military service.

December 21, 2020: Acting Manhattan U.S. Attorney Announces $40.5 Million Settlement with Durable Medical Equipment Provider Apria Healthcare for Fraudulent Billing Practices

Authorities announced a $40.5 million settlement of a fraud lawsuit against Apria Healthcare Group, Inc. and its affiliate, Apria Healthcare LLC (together, "Apria"), a large durable medical equipment ("DME") provider with approximately 300 branch offices located throughout the United States. The lawsuit alleges, among other claims, that Apria submitted false claims to federal health programs, including Medicare, Medicaid, and TRICARE, seeking reimbursement for the rental of costly non-invasive ventilators ("NIVs") to program beneficiaries who were not using the NIVs such that the devices were not medically necessary or that involved the improper waiver of patient co-insurance payments. Under the settlement, which was approved on December 18 by U.S. District Judge Edgardo Ramos, Apria agreed to pay a total sum of $40.5 million, with $37,632,789.89 being paid to the United States and the remaining amount to be paid to various states. As part of the settlement, Apria also made extensive factual admissions regarding its conduct. Apria improperly waived co-pays for several Medicare and TRICARE beneficiaries to induce them to rent NIVs.

Preventing and Deterring COVID-19 Fraud

In addition to the aforementioned significant events, the DoD IG has also issued the following reports specific to COVID-19. These reports are available at www.dodig.mil/COVID-19/Reports/:

- Audit of Contracts for Equipment and Supplies in Support of the Coronavirus Disease–2019 Pandemic (DODIG-2021-045), January 21, 2021
- Special Report: Controls Implemented by the Defense Health Agency to Control Costs for TRICARE COVID-19 Related Services (DODIG-2020-125), September 8, 2020
- Special Report: Protecting Patient Health Information During the COVID 19 Pandemic (DODIG-2020-080), April 27, 2020
- COVID-19 Expenditures – Lessons Learned Regarding Awareness of Potential Fraud, Waste, and Abuse Risk, April 6, 2020

Appendices

Appendix A: Abbreviations and Acronyms

ABACUS	Armed Forces Billing and Collection Utilization Solution
ADA	Antideficiency Act
ADC	Administration, Direction, and Control
ADP	Additional Discount Program
AEAN	Aggregate Entry Age Normal
AFC	Army Futures Command
AFMS	U.S. Air Force Medical Service
AFR	Agency Financial Report
AHLTA	Armed Forces Health Longitudinal Technology Application
AIA	American Institute of Architects
AMC	Army Materiel Command
AMEDDC&S	Army Medical Department Center & School
APSR	Accountable Property System of Record
ASD(HA)	Assistant Secretary of Defense (Health Affairs)
BPSP	Business Process Standardization and Policy
BRAC	Base Realignment and Closure
BUMED	Navy Bureau of Medicine and Surgery
CAC	Common Access Card
CARES	Coronavirus Aid, Relief, and Economic Security Act
CCE	Coding and Compliance Editor
CCMD	Combatant Command
CDC	Center for Disease Control and Prevention
CERCLA	Comprehensive Environmental Response, Compensation, and Liability Act
CFO	Chief Financial Officer
CHCBP	Continued Health Care Benefits Program
CHCS	Composite Health Care System
CIP	Construction in Progress
CMS	Centers for Medicare and Medicaid Services
CoC	Council of Colonels and Captains
COTS	Commercial Off-the-Shelf
COVID-19	Coronavirus Disease 2019
CPAM	Cerner Patient Accounting Module
CPD	Cockerell Dermatopathology
CPI	Consumer Price Index
CPT	Current Procedural Terminology
CRM	Contract Resource Management
CSA	Combat Support Agency
CUECs	Complementary User Entity Controls
CY	Calendar Year
DAI	Defense Agencies Initiative
DAPA	Distribution and Pricing Agreements
DASA FIM	Deputy Assistant Secretary of the Army Financial Information Management
DASD	Deputy Assistant Secretaries of Defense
DATA ACT	Digital Accountability and Transparency Act of 2014
DAWDF	DoD Acquisition Workforce Development Fund
DCIA	Debt Collection Improvement Act of 1996
DCIS	Defense Criminal Investigative Service
DEAMS	Defense Enterprise Accounting and Management System
DFAS	Defense Finance and Accounting Service
DHA	Defense Health Agency
DHAPP	DoD HIV/AIDS Prevention Program
DHP	Defense Health Program
DIMO	Defense Institute for Medical Operations
DLA	Defense Logistics Agency
DM&R	Deferred Maintenance and Repairs
DME	Durable Medical Equipment
DMLSS	Defense Medical Logistics Standard Support
DMMAC	Deputy Military Medical Action Council
DoD	Department of Defense
DoDI	Department of Defense Instruction
DOJ	Department of Justice
DOL	Department of Labor
DTF	Dental Treatment Facility
EHR	Electronic Health Record
EIC	External Independent Contractor
ELCs	Entity-Level Controls
EOP	Executive Office of the President
ERP	Enterprise Resource Planning
FADs	Funding Authorization Documents
FASAB	Federal Accounting Standards Advisory Board
FBwT	Fund Balance with Treasury
FCI	Facility Condition Index
FECA	Federal Employees' Compensation Act
FEDVIP	Federal Employees Dental and Vision Insurance for Program
FEGLI	Federal Employee Group Life Insurance
FEHB	Federal Employee Health Benefit
FFATA	Federal Funding Accountability and Transparency Act of 2006
FFMIA	Federal Financial Management Improvement Act
FFRDC	Federally Funded Research and Development Centers
FGB	GFEBS Functional Governance Board
FISMA	Federal Information Security Modernization Act
FLTCIP	Federal Long-Term Care Insurance Program
FMFIA	Federal Managers' Financial Integrity Act
FMR	Financial Management Regulation
FSRE	Financial Statement Reporting Entity
FTEs	Full-Time Equivalents
FWC	Future Workers' Compensation
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
GAFS-R	General Accounting and Finance System – Reengineered
GEHA	Government Employees Health Association
GFEBS	General Funds Enterprise Business System
GGB	GFEBS Governance Board
GL	General Ledger
GMRA	Government Management Reform Act
GONE Act	Grants Oversight and New Efficiency Act
GPP&E	General Property, Plant and Equipment

GPRA	Government Performance and Results Act
GPRAMA	Government Performance and Results Modernization Act of 2010
GSA	General Service Administration
HA	Health Affairs
HAFC	Health Affairs Functional Champion
H-CAHPS	Hospital Consumer Assessment for Healthcare Providers and Systems
HCPCS	Healthcare Common Procedure Coding System
HHS	Health & Human Services
HJF	Henry M. Jackson Foundation
HMO	Health Maintenance Organization
HRM&P	Health Resources Management and Policy
HRP&O	Health Readiness Policy and Oversight
HSP&O	Health Services Policy and Oversight
I&RP	Inventory and Related Property
IBNR	Incurred but not reported
ICO	Internal Controls Over Operations
ICOFR-FR	Internal Controls Over Financial Reporting-Financial Reporting
ICOFR-FS	Internal Controls Over Reporting Financial Systems
IMR	Individual Medical Readiness
iRAPT	Invoice Receipt, Acceptance and Property Transfer
IT	Information Technology
IUS	Internal Use Software
IUSID	Internal Use Software in Development
JCS	Joint Chiefs of Staff
JOES-C	Joint Outpatient Experience Survey – Clinician and Group Consumer Assessment of Healthcare Providers and Systems
KSA	Knowledge, Skills, and Abilities
M2	MHS Mart
MAC	Medical Affirmative Claims
MAIS	Major Automated Information System
MCSCs	Managed Care Support Contractors
MEDCOM	U.S. Army Medical Command
MERHCF	Medicare-Eligible Retiree Health Care Fund
MHS	Military Health System
MHSER	Military Health System Executive Review Board
MILCON	Military Construction
MOU	Memorandum of Understanding
MPA	Military Personnel Appropriations
MPG	Michigan Physicians Group, P.C.
MRDC	Medical Research and Development Command
MSA	Medical Service Accounts
MTF	Military Treatment Facility
NCR	National Capital Region
NCR MD	National Capital Region Medical Directorate
NDAA	National Defense Authorization Act
NDS	National Defense Strategy
NHE	National Health Expenditures
NHRC	Naval Health Research Center
NIST	National Institute of Standards and Technology
NIV	Non-Invasive Ventilators
NMHM	National Museum of Health and Medicine
NOAA	National Oceanic & Atmospheric Administration
O&M	Operations and Maintenance
OACT	Office of the Actuary
OASD(HA)	The Office of the Assistant Secretary of Defense for Health Affairs
ODO	Other Defense Organizations
OGC	Office of General Counsel
OIG	Office of Inspector General
OM&S	Operating Materiel & Supplies
OMB	Office of Management and Budget
OPM	Office of Personnel Management
OSD	Office of the Secretary of Defense
OTSG	Office of the Surgeon General
OUSD(C)	Office of the Under Secretary of Defense (Comptroller)
PDASD	Principal Deputy Assistant Secretary of Defense
PEPFAR	President's Emergency Plan for AIDS Relief
PFAS	Perfluoroalkyl and Polyfluoroalkyl Substances
PHS	Public Health Service
PI	Program Integrity
PIIA	Payment Integrity Information Act of 2019
PIP	Patient identification process
PMO	Project Management Office
POG	Process Owner's Group
POM	Program Objective Memorandum
PP&E	Property, Plant and Equipment
PPA	Prompt Payment Act
PPO	Preferred Provider Organization
PRV	Plant Replacement Value
RCRA	Resource Conservation and Recovery Act
RDT&E	Research Development Test & Evaluation
RevX	Revenue Cycle Expansion
RSL	Remaining Service Life
S&P	Standards and Policies
SAP	Systems Applications and Products
SARA	Superfund Amendments and Reauthorization Act
SBR	Statement of Budgetary Resources
SCG	System Change Group
SCNP	Statement of Changes in Net Position
SDP	Standard Discount Program
SECDEF	Secretary of Defense
SFFAS	Statement of Federal Financial Accounting Standards
SL	Straight Line
SMA	Service Medical Activity
SME	Subject Matter Expert
SMMAC	Senior Military Medical Advisory Council
SMS	Sustainment Management System
SNC	Statement of Net Cost
SOA	Statement of Assurance
SOC 1	System and Organization Controls
SOF	Statement of Financing
SSO	Stand-Alone Organizations
STARS-FL	Standard Accounting and Reporting System – Field Level
TBD	To Be Determined
TED	TRICARE Encounter Data
TEDS	TRICARE Encounter Data Set
tFIC	Technical Financial Information Council
TFM	Treasury Financial Manual
TI	Treasury Index
TNC	Treasury Nominal Coupon Issues
TPC	Third Party Collections
TPCP	Third-Party Collection Program

TPharm	TRICARE Pharmacy Program
TPR	TRICARE Prime Remote
TRR	TRICARE Retired Reserve
TRS	TRICARE Reserve Select
TSCA	Toxic Substances Control Act
TSOB	The Shape of Behavior
TYA	TRICARE Young Adult
UBO	Uniform Business Office
UDO	Undelivered Order
UMB	Unified Medical Budget
USACE	United States Army Corps of Engineers
USAID	United States Agency for International Development
U.S.C.	United States Code
USCG	United States Coast Guard
USD(P&R)	Under Secretary of Defense for Personnel and Readiness
USFHP	Uniformed Services Family Health Plan
USSGL	United States Standard General Ledger
USUHS	Uniformed Services University of the Health Sciences
VA	Veterans Affairs
VHA	Veterans Health Administration
WAWF	Wide Area Workflow
WRNMMC	Walter Reed National Military Medical Center

We would like to hear from you

We would like to hear from you about our FY 2021 Agency Financial Report. Did we present information in a way you could use? What did you like best and least about our report? How can we improve our report in the future?

Please send written comments to:

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