ADDENDUM A, OTHER INFORMATION

Other Information provides additional details that support the Fiscal Year (FY) 2013 Department of Defense (DoD) Agency Financial Report (AFR). This addendum includes the following sections:

Inspector General's Summary of Management and Performance Challenges for FY 2013

Managers' Internal Control Program

Improper Payment and Payment Recapture Programs

INSPECTOR GENERAL'S SUMMARY OF MANAGEMENT AND PERFORMANCE CHALLENGES FOR FY 2013

INTRODUCTION

The *Reports Consolidation Act of 2000* requires that the Agency Financial Report (AFR) include a statement, prepared by the Department's Inspector General (IG), which summarizes what the IG considers to be the most serious management and performance challenges facing the Department, along with a brief assessment of the Department's progress made in addressing those challenges. In FY 2013, the IG identified the following seven categories of management and performance challenges facing the Department:

1. Financial Management

2. Acquisition Processes and Contract Management

3. Joint Warfighting and Readiness

4. Cyber Security

5. Health Care

6. Equipping and Training Afghan Security Forces

7. The Nuclear Enterprise

Chairman of the Joint Chiefs of Staff GEN Martin E. Dempsey talks with U.S. Marine Corps drill instructors at the 4th Recruit Training Battalion, Parris Island, SC, on March 21, 2013. The 4th Recruit Training Battalion is a female-only unit at Parris Island.

DoD photo by Master Sgt. Charles Marsh, U.S. Air Force

SUMMARY OF IDENTIFIED CHALLENGES

The following tables report the IG's summary of the challenges, an assessment of the Department's progress in addressing these challenges, and the Department's response.

1. IG-Identified Challenge: Financial Management

1-1A. Achieving Financial Statement Audit Readiness	IG Summary of Challenge

The Department's financial management challenges impair its ability to provide reliable, timely, and useful financial and managerial data to support operating, budgeting, and policy decisions. Gaps in the financial framework harm the accuracy, reliability, and timeliness of budgetary and accounting data and financial reporting, reducing the effectiveness of decisions made by leaders at all levels. Key to solving the Department's financial management problems is the production of auditable financial statements and receiving unqualified opinions on them.

Achieving auditable financial statements is a longstanding and daunting task. The success of the DoD financial improvement and audit readiness effort depends on the Department's ability to:

- Resolve material internal control weaknesses to ensure internal controls are properly designed, properly implemented, and working effectively.

- Monitor and resolve new material internal control weaknesses identified as part of ongoing readiness efforts.

- Sustain improvement in internal controls and systems to provide consistent and repeatable financial data used in decision making and reporting.

- Effectively develop and implement the financial-improvement effort by monitoring DoD progress in achieving milestones, developing comprehensive improvement initiatives across DoD functional areas, and holding managers accountable for the timely implementation of those efforts.

Congress requires the Department to validate as audit-ready the DoD Statement of Budgetary Resources (SBR) and the other DoD financial statements by September 30, 2014, and September 30, 2017, respectively. Meeting those deadlines will be a significant challenge for the Department. Furthermore:

- *Public Law 111-383, Section 881*, requires the Department to establish interim milestones to achieve audit readiness of its financial statements earlier than September 30, 2017. These interim milestones for Military Departments and Defense Components call for the achievement of audit readiness for each major element of the Statements of Budgetary Resources (SBR), such as "civilian pay, military pay, supply orders, contracts, and the funds balance with the Treasury."

- *Public Law 112-81, Section 1003*, requires the Department to have a plan that includes interim objectives and a schedule of milestones for each Military Department and for the Defense agencies, to support the goal of validating the SBR as audit-ready by September 30, 2014. The Department must aggressively pursue the development and implementation of comprehensive improvement initiatives and must monitor progress according to interim milestones. The Department may need to revise these initiatives and milestones as it identifies additional deficiencies and corrective actions, as a result of DoD's iterative Financial Improvement and Audit Readiness (FIAR) process.

- *Public Law 112-239, Section 1005(b)(1)*, requires that the plans to achieve audit readiness of the SBR "by September 30, 2014, include steps to minimize one-time fixes and manual work-arounds, be sustainable and affordable, and not delay the full auditability of financial statements." Meeting the accelerated 2014 milestone for auditability of the SBR will be a challenge for the Department.

The Department must continue to develop and implement a comprehensive plan that identifies the interim objectives and schedule of milestones to achieve audit readiness of the SBR for the Working Capital Fund and General Funds. The interim milestones must address the existence and completeness of each major category of DoD assets, which includes military equipment, real property, inventory, and operating material and supplies.

Additionally, Section 881 of Public Law 111-383 requires the Department to examine the costs and benefits of alternative approaches to valuing its assets, develop remediation plans when interim milestones cannot be met, and identify incentives to achieving auditability by September 30, 2017.

1-1B. Achieving Financial Statement Audit Readiness	IG Assessment of Progress

Although the Department is far from reaching an unqualified opinion on its financial statements, it has made progress. The DoD senior leadership has placed an increased emphasis on achieving this goal. We believe this increased emphasis is essential to the Department's ability to meet its internal milestones, as well as the 2014 and 2017 audit readiness mandates.

Despite pervasive and longstanding Department financial management problems, the Army Corps of Engineers and various Defense agencies, such as the Defense Commissary Agency and Defense Contract Audit Agency, and the Military Retirement Fund, have received unqualified audit opinions. The Department must sustain its achievements as well as advance in the remaining significant areas.

The Department continues to make progress toward meeting the 2014 audit readiness goal of the SBR; however, it is still uncertain whether the Department will meet the 2014 goal. The Department continues to learn and improve from the DoD IG audits of the SBR for the U.S. Marine Corps (USMC), the first Military Service to undergo such an audit. The USMC encountered many challenges during this first type of audit, which resulted in disclaimers of opinion in FY 2010 and FY 2011. The USMC is undergoing its third audit, and progress was seen in the Corp's ability to produce supporting documentation on historical transactions within the Schedule of Budgetary Activity (SBA). The USMC, the Navy, and the Department are using this experience to correct weaknesses, as well as prepare the other Military Services for their eventual SBR audit.

The *May 2013 FIAR Plan Status Report* only addresses audit readiness of certain aspects of the SBR and states that the Department does not expect every Component to achieve an SBA clean audit opinion in FY 2015. The Department reported in the November 2011 FIAR Plan update, and continued to report in the May 2013 FIAR Plan update, that it had significantly changed its audit goals to include achieving audit readiness of the General Fund SBR by the end of FY 2014, in addition to achieving audit readiness of all DoD financial statements by the end of FY 2017. However, in the November 2012 FIAR Plan update, the Department reported it would limit first-year SBR audits in FY 2015 to audits of schedules containing only current-year appropriation activity (i.e., a Schedule of Budgetary Activity).

Additionally, in the May 2013 FIAR Plan update, the Department reported that the initial audits of the General Fund Schedule of Budgetary Activity will not include balances from prior year activity. The Department will also begin audits of the complete SBR only after achieving successful audits of current-year appropriation activity. Meaningful progress in FY 2014 for the SBR audit-readiness goal will be critical, and this will continue to be a high-visibility area.

Addendum A

1-1C. Achieving Financial Statement Audit Readiness	Department Response

The Department generally agrees with IG's assessment of DoD's progress in achieving audit readiness. Significant progress continues to be made, and the Department is fully committed to achieving audit readiness on its full financial statements by September 30, 2017.

The FIAR Strategy focuses on achieving audit readiness of the Statement of Budgetary Resources (SBR) by September 30, 2014. Audit readiness means the Department has improved financial practices, processes, and systems, and strengthened internal controls so that there is reasonable confidence that the information can withstand an audit by an independent auditor.

The scope of FY 2015 audits will be on current-year information contained in the SBR. The Department refers to current year information of the SBR as the Schedule of Budgetary Activities or SBA. The initial General Fund SBA audits will not include balances from prior year activity. The U.S. Marine Corps audit, which has been audited by the DoD IG, employed this same approach. The Government Accountability Office and the DoD IG have been fully briefed and agree that focusing FY 2015 audits on current year information is a cost-effective and sensible path to full audit readiness. The Department is developing guidance for achieving Wave 4, full financial statement audit readiness.

Achieving auditable financial statements will help the Department improve processes and make better use of resources. More importantly, auditable financial statements will demonstrate to the American public and Congress that the Department is a good steward of government funds. Although the Department is diligently working to achieve SBR audit readiness by the end of FY 2014 and begin SBA audits in FY 2015, several challenges exist outside the Department's control that have the potential to impede progress.

For more information, refer to the *FIAR Plan Status Report*.

1-2A. Modernizing Financial Systems (Enterprise Resource Planning)	IG Summary of Challenge

To develop effective financial-management processes throughout the Department, the Department has begun to implement new financial management systems and business processes. We believe properly planned and integrated systems, with strong internal controls, are critical to providing useful, timely, and complete financial management data and to achieving auditability. Timely and effective implementation of the enterprise resource planning systems (ERPs) is critical for the Department to achieve its financial improvement and audit-readiness goals.

The Department noted in the latest FIAR update that the ERPs continue to be essential to the Department's audit-readiness efforts. However, not all ERPs will be deployed by the 2014 and 2017 readiness deadlines. This will require the Department to continue to rely on legacy systems.

1-2B. Modernizing Financial Systems (Enterprise Resource Planning)	IG Assessment of Progress

The Department plans to spend about $15 billion to develop and implement ERPs. These systems have experienced cost increases and schedule delays. The Department noted that some ERPs will not be fully deployed by the 2014 and 2017 audit-readiness dates, and therefore it must continue to rely on legacy systems. This will increase the risk that the SBR, or a schedule of current year budget activity, will not be auditable by September 30, 2014,

and that the Department will not meet the goal of full financial statement audit readiness by September 30, 2017. Reliance on legacy systems, along with schedule delays and poorly developed, poorly implemented ERPs, will diminish the savings expected from transforming operations through business-system modernization.

Furthermore, without fully deployed ERPs, the Department will be challenged to produce reliable financial data and auditable financial statements without resorting to extreme efforts, such as data calls or manual workarounds, to provide financial data on a recurring basis. For example, the Department reported in the May 2013 FIAR Plan Status Report that the Air Force ERPs will not be fully deployed by 2014. As a result, the Air Force will rely on manual controls and legacy system enhancements to meet the goal of SBR audit readiness by September 30, 2014.

The Department has not reengineered its business processes to the extent necessary; instead, it has often customized commercial ERPs to accommodate existing processes. This creates a need for system interfaces and weakens controls built into the ERP system. The ERPs were designed to replace numerous subsidiary systems, reduce the number of interfaces, standardize data, eliminate redundant data entry, and provide an environment for end-to-end business processes, while being a foundation for sustainable audit readiness. However, the numerous interfaces between the ERP system and existing systems may be overwhelming and inadequately defined. Each interface presents a risk that the system might not function as designed, and each prevents the linking of all transactions in an end-to-end process. The Department needs to ensure ERP system development addresses the required business processes and functions.

Without the effective and timely development and implementation of ERP systems, and without senior-level governance, the Department will continue to struggle to improve its financial management processes and provide accurate, timely, and meaningful financial management information for internal and external users and achieve long-term sustainability of the financial-management improvements. Recent audits continue to find that system program managers have not configured systems to report U.S. Government Standard General Ledger (USSGL) financial data using the DoD Standard Financial Information Structure (SFIS).

Additionally, other audits have found that the Department has not sufficiently reengineered its business enterprise architecture processes nor incorporated the functionality in ERP systems. The Department has established certification requirements, and the Deputy Chief Management Officer and Deputy Chief Financial Officer have established validation and certification procedures for implementing SFIS requirements and ensuring business process reengineering has taken place. However, these procedures were not stringent enough to ensure compliance. The Department continues to improve its validation and certification procedures.

1-2C. Modernizing Financial Systems (Enterprise Resource Planning)	Department Response

The Department is committed to supporting improvements to financial processes through the implementation of ERP systems. In support of these efforts, the Department has been working diligently to improve business processes, oversight of the development of the ERPs, and implementation of formal business process reviews in support of auditability.

While it is true that legacy systems will continue to be employed during the development and full deployment of the ERPs, the implementations that have already occurred throughout the Department have resulted in the ability to phase out dozens of legacy systems. Several of the Department's ERPs have been or will be implemented to support the 2017 auditability goal. However, where we are dependent on legacy systems, the Components' Financial Improvement Plans incorporate actions necessary to ensure that accurate, reliable financial information is reported.

Modernizing DoD business systems is a key aspect of our overall effort to achieve and sustain auditability. The Department plans to achieve the audit goals with a combination of both target and legacy systems. While taking pro-active steps to align individual ERP programs with auditability outcomes, we also are focused on delivering audit-ready processes and controls that will remain outside the ERP systems. This will allow us to develop a sustainable business environment that can be cost-effectively audited.

The ERP programs, by their very nature, are designed to:

- Handle transactions in a defined end-to-end process;

- Enforce process and execution standardization among implementing organizations;

- Manage consolidated business data in a single repository that allows centralized access control, and

- Facilitate the flow of information both within an organization and with external stakeholders.

These design principles within the ERP directly enable capabilities essential to auditability, such as the ability to trace all transactions from source to statement; the ability to recreate a transaction; documented, repeatable processes and procedures; demonstrable compliance with laws, regulations and standards; and a control environment that is sufficient to reduce risk to an acceptable level.

Essentially, ERPs are acquired with industry best practices/"to-be" processes embedded within them. Each of the Department's ERP programs went through significant, up-front blueprinting and gap analysis to determine which configuration or customization was necessary for the system to work within its particular business environment. The Department has focused on properly enforcing compliance with the target financial management environment, built on a backbone of the core ERP systems and aligned with the Business Enterprise Architecture's end-to-end processes.

The Department's new investment management process will ensure:

- Investments are aligned to strategies;

- Allow the Department to make more informed investment decisions;

- Eliminate legacy systems that are no longer required;

- Enhance interoperability, and

- Help the Department transform to an environment where business applications can be rapidly deployed on a common computing infrastructure.

The new process also will ensure that each investment is an appropriate use of taxpayer dollars and aligns to the Department's architecture and our shared goal of delivering agile, effective and efficient business solutions that support and enable our warfighters.

To implement this new investment management process, the Deputy Chief Management Officer issued guidance to ensure that the Department continues to treat its business system investments with the firmness of purpose and discipline that will enable cost savings to be redirected to critical operational needs of the warfighter. The guidance, now updated annually, creates an integrated business framework to align broad Departmental strategy with functional and organizational strategy, all the way to system implementations. This framework utilizes new plans, called Functional Strategies and Organizational Execution Plans, to help achieve the Department's target business environment.

The Department's financial management functional strategy includes compliance and standards related to financial management strategic initiatives, such as SFIS/Standard Line of Accounting, US Standard General Ledger, and FIAR audit readiness. As part of each Service or Agency's Organizational Execution Plan-Financial Management, each of the strategic initiatives must be addressed with reference for compliance. Additionally, each system owner is required

to update the DoD Information Technology Portfolio Repository with compliance to both the Business Enterprise Architecture and SFIS standards as part of the Investment Review Board process.

1-3A. Improper Payments	IG Summary of Challenge

Improper payments, a longstanding problem in the Department, are often the result of unreliable data and/or a lack of adequate internal controls, which increases the likelihood of fraud. As a result, the Department lacks assurance that billions of dollars of annual payments are disbursed correctly. The Department's inadequate financial systems and controls hamper its ability to make proper payments. In addition, the pace of operations and volume of Department spending create additional risk for improper payments, and both hinder the Department's ability to detect and recover those improper payments.

The Department faces difficulties in the completeness and accuracy of its improper payment reviews and the information reported. However, problems remain, including the auditability of the SBR. This leaves the Department unable to reconcile outlays to the quarterly or annual gross outlays reported in the SBR to ensure all required payments for reporting purposes have been captured. In addition, during a reconciliation of FY 2012 outlays, the Department identified $12.3 billion in outlays that should have been reviewed for improper payments, but were not. These areas require improvement before the Department will be able to provide complete and accurate information on its estimated amount of improper payments.

1-3B. Improper Payments	IG Assessment of Progress

Although the Department made strides to improve the identification and reporting of improper payments and took many corrective actions to implement recommendations made by the DoD IG, more work is needed to improve controls over payments processed throughout the Department.

The Department improved its program during FY 2012, including statistically projecting improper-payment error rates for contract and vendor payments, as well as reviewing additional military health benefit programs that previously had not been included in improper-payment reviews. However, there are indications that the amount of estimated improper payments may be understated. For example, a March 2013 audit showed that during a DoD reconciliation of FY 2012 outlays, the Department identified $12.3 billion in outlays that should have been reviewed for improper payments but were not. The $12.3 billion is lower than previous unreconciled amounts, but improper payment reviews of these outlays would likely increase improper payment amounts reported.

Additionally, the estimated amount of improper payments for the Department's commercial pay program for FY 2012 ($100.1 million) is significantly less than the Defense Logistics Agency (DLA) Troop Support's recovery of payments on one subsistence contract from December 2005 through September 2011, which totaled $756.9 million. The DLA said that recoveries had averaged approximately $21 million per month since March 2012. Additional sources included the Defense Contract Audit Agency's audits and contracting officers' subsequent recovery actions. In addition, the April 1, 2012 through September 30, 2012, DoD Inspector General Semiannual Report to Congress, reported that Contracting Officers initiated actions during this period to disallow $692.0 million of costs questioned in Defense Contract Audit Agency (DCAA) contract audits.

We commend the Department on aggressively pursuing recovery of identified improper payments, but unless it continues to improve its methodology for reviewing all its disbursements, it will likely underestimate overpayments and, as a result, miss opportunities to collect additional improper payments.

1-3C. Improper Payments	Department Response

The Department appreciates the DoD IG's recognition of DoD's improvements in identifying, reporting, and recovering improper payments and in implementing corrective actions. The Department is committed to complying with all laws and regulations established to reduce improper payments.

The $12.3 billion in outlays that the IG reports were not reviewed for improper payments, but possibly should have been, has dropped precipitously over the past several years and now represents a very small fraction of Department's total outlays. The Department is marching toward audit readiness for the Schedule of Budgetary Activity by the end of FY 2014 and the longer-term goal of full financial statement audit readiness by the end of FY 2017.

We do not agree with the following information reported by the DoD IG:

- The $756.9 million the IG reported as an improper payment, with recoveries averaging approximately $21 million per month, did not result from an improper payment, but rather is the result of a contract price adjustment.

- The $692 million in contract questioned costs identified by DCAA, or any other audit entity, are not a result of an improper payment, but are decisions made by the Contracting Officer based on audit findings and recommendations driven by contract terms and conditions and Federal Acquisition Regulations.

2. IG-Identified Challenge: Acquisition Processes and Contract Management

2-1A. Enhancing the Acquisition Workforce	IG Summary of Challenge

The Department senior leadership continues to recognize the importance of fielding a capable acquisition workforce to manage and oversee DoD acquisition and contracting. To accomplish the acquisition mission, the Department is placing greater emphasis on developing a higher-quality workforce with the needed competencies.

Even though the Defense acquisition workforce has grown over the last few years, the Department continues to struggle to rebuild an acquisition workforce that is trained and equipped to oversee DoD acquisitions. The Department should continue to provide developmental opportunities to ensure that acquisition personnel can manage complex programs. Regardless of the looming decline in the Defense budget, the acquisition workforce will continue to be vital in providing the warfighters with new capabilities. Previous Defense budget cuts significantly reduced the capability of the acquisition workforce; the Department should maintain focus on strengthening the acquisition workforce throughout the lean financial years expected ahead.

On April 24, 2013, the Under Secretary of Defense (Acquisition, Technology, and Logistics) (USD(AT&L)) announced Better Buying Power 2.0, aimed at obtaining greater efficiencies and productivity in defense spending. The Better Buying Power (BBP) 2.0 outlined four initiatives to meet the objective of focusing on training and improvement of the acquisition workforce.

These BBP initiatives include:

- Establishing higher standard for key leadership positions
- Establishing stronger professional qualification requirements for all acquisition specialties
- Increasing the recognition of excellence in acquisition management
- Continuing to increase the cost consciousness of the acquisition workforce – change the culture

2-1B. Enhancing the Acquisition Workforce	IG Assessment of Progress

The Department has filled 7,700 new acquisition positions since 2008, and as of the second quarter of 2013, the acquisition workforce comprises more than 152,800 personnel. The Defense Acquisition Workforce Development Fund budget request for $276.2 million in FY 2014 supports the Department's shift from primarily recruiting and hiring to training and improvement in the qualifications and experience of the acquisition workforce. However, budget constraints raise questions as to whether the Department will be able to sustain these initiatives. Sustained commitment and management attention is essential to ensuring the improvements to the acquisition workforce are not lost or diminished.

2-1C. Enhancing the Acquisition Workforce	**Department Response**

The Department concurs with the IG's assessment.

2-2A. Weapon System Acquisition	IG Summary of Challenge

The Department remains challenged in its management of Major Defense Acquisition Programs (MDAPs), which have decreased in number. As of December 2012, the Military Departments reported 78 Acquisition Category I Programs (MDAPs), which is down from the 83 programs reported in December 2011.

Although the performance of no two acquisition programs is the same, and a good number of them operate within cost and schedule constraints, there are still too many programs with significant cost growth and delays in delivering capabilities. Our audits have identified programs that did not complete required testing, identify the correct procurement quantity, or define capability requirements. The Department should continue to look for a better balance between its limited resources and the capabilities needed to succeed in current and future conflicts. As budgets come under increasing scrutiny under sequestration, the Department is challenged to evaluate the merits of all programs as to their usefulness and the need for further program adjustments or terminations to remain within budget constraints.

2-2B. Weapon System Acquisition	IG Assessment of Progress

Through leadership at the highest levels, the Department has demonstrated its commitment to addressing shortcomings identified in the management of weapon system acquisitions. The Department continues to reprioritize and rebalance its investments in weapon systems and has made progress in improving efficiency.

The *Department's FY 2014 Annual Performance Plan* goals show the Department's commitment to containing weapon system acquisition program cycle time and cost by assessing the root causes of weapon system acquisition outcomes and monitoring the effectiveness of its acquisition policies.

In BBP 2.0, the USD(AT&L) mandated affordability as a requirement and emphasized the affordability constraints imposed in the first Better Buying Power effort started in September 2010. The BBP 2.0 also states that the Department will focus on controlling costs throughout the product lifecycle, using the following initiatives:

- Implementing "should cost" based management

- Eliminating redundancy within warfighter portfolios

- Instituting a system to measure the cost performance of programs and institutions and to assess the effectiveness of acquisition policies

- Building stronger partnerships with the requirements community

- Increasing the incorporation of defense exportability features in initial designs

The Department, as it continues to make the hard decisions about what is affordable, is beginning to apply extra scrutiny to weapon systems that are behind schedule and over cost. Senior leadership has recently demonstrated sound stewardship by eliminating MDAPs that were underperforming or over budget, or whose value given the continuing investment was in question.

2-2C. Weapon System Acquisition	Department Response

The Department concurs with the IG's assessment. In addition to the initiatives discussed by the IG, the Department has taken a number of steps to improve the operation of the defense acquisition system in order to deliver more capability to the warfighter for less than it has in the past. The USD(AT&L) directed a major revision to *DoD Instruction (DoDI) 5000.02*, which describes the operation of the defense acquisition system.

The revision, which is expected to be signed by the end of calendar year 2013:

- Decreases emphasis on "rules" and increases emphasis on process intent and thoughtful program planning.

- Provides program structures and procedures tailored to the dominant characteristics of the product being acquired and to unique program characteristics (e.g., risk and urgency).

- Increases emphasis on planning effective business arrangements and overall program affordability.

- Enhances the discussion of program management responsibility and key supporting disciplines to include systems engineering, developmental testing and cost estimating.

2-3A. Contract Management	IG Summary of Challenge

The Department continues to struggle to consistently provide effective oversight of its contracting efforts. The Department's continuing contracting deficiencies include obtaining adequate competition in contracts, defining contract requirements, overseeing contract performance, obtaining fair and reasonable prices, and maintaining contract documentation for contract payments.

The Department relies heavily on contractors to provide acquisition management and contract support functions, which often includes support to acquisition planning, requirement determinations, contract award determinations, performance reviews, bid analysis, cost assessments, and other contract monitoring functions. The Department's increased use of contractors as acquisition support highlights DoD's shortcomings. Service contracts constitute more than 50 percent of the Department's contract spending.

The Department faces several challenges in contract oversight and administration. Our audits continue to identify that without proper oversight, the Department cannot be certain that contractors are performing in accordance with contract requirements, cannot support payments of award or incentive fees, cannot support the certification of invoices for services performed, and cannot ensure that services are performed, leaving the Department vulnerable to increased fraud, waste, and abuse.

The Department continues to face challenges in obtaining fair and reasonable prices for parts. Audits first started identifying problems with price-based acquisition and commercial pricing in the late 1990s, and it was not until 2008 that legislative changes allowed contracting officers to request information on labor costs, material costs, and overhead rates for commercial items.

More recently, the Department has moved to new performance-based logistics (PBL) arrangements, which have added a new challenge to obtaining fair and reasonable prices for parts, since the Services are now procuring parts from the weapons systems contractors instead of other sources, such as the Defense Logistics Agency. Often these parts are purchased unnecessarily and at higher prices rather than utilizing existing DLA inventory.

2-3B. Contract Management	IG Assessment of Progress

The Department continues to strengthen contracting and has issued policy, procedures, and guidance addressing current contracting challenges. The Department began the Better Buying Power effort in 2010 and continued with the second phase of the initiative, BBP 2.0, in April 2013. The BBP 2.0 has seven areas of focus, and three of them help the Department address contract-management challenges: Promoting effective competition; Improving tradecraft in acquisition of services; and Incentivizing productivity and innovation in industry and Government

To promote effective competition, BBP 2.0 emphasizes competition strategies, creating and maintaining competitive environments and increasing small business roles and opportunities among other initiatives. When competition is applied effectively, it results in lower costs to the Government, greater innovation from industry, and added savings to the taxpayer.

Because service contracts make up so much of the Department's purchases, the BBP 2.0 area of improving tradecraft in the acquisition of services is very important. The Department will focus on assigning senior managers for the acquisition of services, improving requirements definitions and preventing requirements creep, and strengthening contract management outside the normal acquisition chain among other initiatives.

As part of its area of incentivizing productivity and innovation in Industry and Government, BBP 2.0 has an initiative to increase effective use of PBL and states that the history of PBL contracting demonstrates the Department can achieve improved readiness at significant savings if PBL arrangements are properly structured and executed. The success of the PBL arrangement depends on the workforce having the expertise and support to properly develop and implement these arrangements and continued emphasis to utilize lower cost inventory already on hand rather than continuing to purchase parts from contractors.

2-3C. Contract Management	Department Response

The Department agrees with the IG's summary of challenges and assessment of progress and continues to work aggressively to resolve the long-standing material weaknesses in contract management. These key initiatives include:

The USD(AT&L) has established a Services Acquisition (SA) Directorate to oversee and improve services acquisitions, which constitute more than half of DoD's contracted obligations. Planning, managing, and overseeing contractors who perform service functions demands a different approach than that used to oversee contractors who are developing our weapon systems. The SA Directorate is leading the improvement of DoD's tradecraft in acquisition of services, which is a key part of the Department's BBP efficiencies initiative. To deliver better value to both the warfighter and the taxpayer while improving the way the Department does business, the Services Acquisition directorate is establishing:

- A stand-alone DoD instruction solely for the acquisition of services.
- Functional Domain Experts to manage services portfolios.
- Better services requirements development processes and tools.
- Service Requirement Review Boards and Tripwires to better manage and validate requirements.
- "Should cost" methodology for services acquisitions.
- Appropriate metrics to actively manage services acquisitions.

Additionally, the Department is working on strengthening services contract management outside of the normal acquisition chain (e.g., installations and commands) as well as developing processes to ensure individuals who are not Defense Acquisition Workforce Improvement Act certified, and who are involved in services acquisitions, are properly trained. This new management structure and training capabilities, coupled with changes in the way the Department analyzes and tracks services acquisitions, will allow us to continuously improve, from requirements definition to closeout, focusing on outcome-based capabilities.

- Continued use of "peer reviews" to improve the quality of contracting processes across the Department and facilitate cross-sharing of best practices and lessons learned.

- On December 6, 2012, the Director of Defense Procurement and Acquisition Policy issued a memorandum, entitled "Service Acquisition Workshop." This policy requires Senior Officials to immediately ensure that all multi-functional teams that support service acquisition requirements valued at $1 billion or more participate in a Service Acquisition Workshop (SAW) as a prerequisite to Office of the Secretary of Defense (OSD) review/approval of the service acquisition strategy. Additionally, Senior Officials were encouraged to consider mandating SAWs for services acquisitions valued at $100 million or more.

- On January 14, 2013, the USD(AT&L) issued a memorandum, entitled "Traceability of Contract Execution Expenditures for Services," that highlights the importance of tracing contract expenditures for services. To improve tracking of service contract commitments and obligations, all DoD Components must update their acquisition and financial procedures and systems to ensure all purchase requests include a four-digit Product Service Code at a line item level of detail.

- On March 12, 2013, the Director of Defense Pricing issued a memorandum, entitled "Contract Business Analysis Repository," that informs the DoD Components about the capabilities of Contract Business Analysis Repository (CBAR) and instructs them to begin loading business clearance information into CBAR effective June 24, 2013. The CBAR facilitates the sharing of information among DoD contracting officers and assists them during their preparation for negotiations with contractors to support getting the best deal for the warfighters and taxpayers.

- All Components are now participating in using the DoD Contracting Officer Representative Tracking (CORT) tool with over 30,000 active Contracting Officer's Representative (COR) users. In April 2013, the CORT tool was successfully transitioned to the Wide Area Workflow (WAWF) portal as its permanent hosting platform for the CORT. The CORT is a web-based tool that enables military departments and defense agencies to manage nomination, training and tracking of their respective cadres of CORs and the contract(s) assigned to each COR.

- On August 30, 2013, Director, Defense Procurement and Acquisition Policy signed the Services Acquisition Functional Integrated Product Team charter to improve services acquisition via targeted, effective training of services acquisition stakeholders.

3. IG-Identified Challenge: Joint Warfighting and Readiness

3-1A. Joint Warfighting and Readiness	IG Summary of Challenge

U.S. military forces are entering a time of transition. In the years since the terrorist attack on September 11, 2001, the war in Iraq has ended and the lead security responsibility in Afghanistan is transitioning to the Afghan government. Military forces are engaged in a strategic rebalance to the Asia-Pacific region while continuing to maintain enough presence in the Middle East to protect our national interests. At the same time, fiscal deficits and economic problems are driving reductions in Federal spending, including reduced funding for defense programs. It is critical that the Department continually assess warfighter capabilities and readiness and make the necessary adjustments to ensure our military is agile, flexible, and ready for the full range of contingencies.

The Department will face many challenges as it continues force reductions while striving to achieve a modern, ready, and balanced force to meet future requirements. Among these challenges are a decreasing budget, a drawdown of forces from Afghanistan, the need to reset equipment and personnel across the Services, a return to full-spectrum training, and a rebalance of force structure and investments toward the Asia-Pacific and Middle East regions.

The new budget reality is being felt across the Department, especially in areas such as maintenance of existing equipment and systems, the fielding and implementation of new systems, and the frequency and extent of training and exercises. The impact of the sequestration was felt almost immediately as the Navy adjusted repair and overhaul schedules for ships and the Air Force began restricting flying hours for squadrons. The Services and the Combatant Commands need to ensure that the impact of the current sequestration, as well as future budget reductions, has minimal impact on the ability to respond to future threats.

The drawdown of forces from Afghanistan will challenge the Department to transition from counterinsurgency operations to full-spectrum operations elsewhere in the world. Therefore, the Department is refocusing training programs to include joint, interagency, and international training aspects; enhancing knowledge of various languages and cultural, ethnic, and religious sensitivities; and training the reserve forces, whose readiness was impaired for the sake of readiness of the deployed forces. The retrograde and reset for equipment will continue to affect the Services over the next several years, as equipment continues to be returned after seeing utilization rates exceeding many of their designed operating parameters. The enhanced focus on the Pacific and Middle East will also challenge the Department as it reaffirms alliances in the region and looks to establish new ones.

3-1B. Joint Warfighting and Readiness	IG Assessment of Progress

The Department must assess warfighter capabilities and readiness across the full range of strategic, operational, and tactical considerations. This includes large questions, such as whether the joint force is capable of achieving the strategic objectives set forth in the *National Security Strategy*, to the tactical focus on individual unit readiness. The Department is making progress in addressing the many difficulties in the drawdown in Afghanistan, resetting equipment, and ensuring the long-term viability of the all-volunteer force. However, the Department must also be ready to address fiscal challenges, starting with the first round of sequestration. There are already reductions in spending for available training hours and needed maintenance and reset needs.

The National Security Strategy released in January 2012 placed increased emphasis on the Pacific theater. This will present challenges to all the Components of the Department as they shift their focus to the Pacific. The armed forces will have to train to fight in conventional and unconventional scenarios, and they will be challenged to do so with diminishing resources,

while maintaining their readiness. The Department will have to provide additional oversight to ensure that the equipment reset process is managed so that only unusable equipment is disposed and new equipment is fielded to the intended users. The Department must also provide the necessary levels of oversight to ensure that forces returning from Afghanistan, and their families, continue to receive the support they need.

As the drawdown continues in Afghanistan, the Department must ensure the reserve Components have the equipment and training necessary in order to meet their missions. For example, we recently reported that the Army officials did not implement procedures to properly account for the transfer and replacement of 239,332 pieces of Army Reserve Component equipment, valued at $5.8 billion. As a result, Army Reserve Components had lost transparency of their equipment transfers and may experience shortages that could hinder their ability to train soldiers and respond to emergencies.

Efforts to redeploy military units around the globe will enable the armed forces to better shape and focus their force structure to provide greater flexibility in responding to threats. The realignment of forces from Okinawa, Japan, to Guam still faces formidable challenges that have increased projected costs and schedules for the planned effort.

3-1C. Joint Warfighting and Readiness	Department Response

Despite our consistently high operations tempo, the Department remains committed to ensuring deployed forces around the globe are trained, equipped, and ready to perform their assigned missions. Deploying capable and ready forces for current operations continues to impact the non-deployed forces' ability to prepare for full spectrum operations. Non-deployed forces are focusing their available training time to prepare for their next mission in support of Operation Enduring Freedom, hedging against execution of other potential contingencies.

The withdrawal of forces from Afghanistan has reduced the stress on forces in the near term; however, fiscal constraints will result in tough decisions on materiel, manpower, and infrastructure could negate the positive aspects expected from the reductions in operational stress. Additionally, even with the reduction of ground forces in the Central Command area of responsibility, it is anticipated the demand for Naval and Air Forces will continue unabated in the near term.

The Department is continually developing and refining comprehensive plans for both resetting and rebalancing the total force, which includes all reserve Component forces, in the most effective and efficient manner possible. We recognize the most important part of maintaining joint warfighting capability and readiness is caring for the all-volunteer force. Finding the proper balance between maintaining readiness, force structure, modernization, fiscal realities, and future threats remains the highest priority of the Department's leadership.

4. IG-Identified Challenge: Cyber Security

4-1A. Cyber Security	IG Summary of Challenge

Cyber security will, for the foreseeable future, continue to be a leading challenge for DoD – the United States' largest Government agency, with buildings and structures at more than 5,000 different locations. Cyber security is the prevention of damage to, protection of, and restoration of computers, electronic communication systems, electronic communications services, wire communication, and electronic communication, including information contained therein, to ensure its availability, integrity, authentication, confidentiality, and non-repudiation. Every day, hackers infiltrate key Government and business computer networks. Government estimates indicate American companies lose $250 billion a year in intellectual property through network intrusions.

According to the Defense Science Board Task Force Report, "*Resilient Military Systems and the Advanced Cyber Threat,*" January 2013, U.S. Military forces are critically dependent on networks and information systems to execute missions. The forces are highly vulnerable if threats to those networks and information systems are not mitigated. For example, hackers take advantage of systems that continuously scan address spaces of target organizations, waiting for unprotected systems to be attached to the network. Attackers also look for computers that are not up to date with patches because they are not frequently connected to the network. The DoD Chief Information Officer stated, "There will never be a time that we can assume a 'comfort' posture." Therefore, it is imperative that DoD leadership challenge its personnel to be ever vigilant and to continuously monitor and protect DoD networks and information systems.

4-1B. Cyber Security	IG Assessment of Progress

Over the last three years, the DoD IG has performed a series of audits on DoD's Information Assurance Vulnerability Management (IAVM) Program. The IAVM process provides positive control of the vulnerability notification process for network assets by requiring Components' receipt acknowledgement and giving deadlines for implementing appropriate countermeasures, depending on the criticality of the vulnerability.

Since our involvement in this key area, we have noted continued progress by the Department. For example, the Department issued the *Chairman of the Joint Chiefs of Staff Instruction (CJCSI) 6510.01F* in February 2011, which updated the roles and responsibilities of the Information Assurance Vulnerability Management Program. The CJCSI 6510.01F also stated that detailed processes will be featured in an upcoming manual. To continue this progress, the Department still needs to update DoD Directive (DoDD) 0-8530.1, Computer Network Defense (CND), January 8, 2001, and DoD Instruction (DoDI) 0-8530.2 "Support to Computer Network Defense (CND)," March 9, 2001. As recent as the second quarter of FY 2013, we have seen that the lack of updated guidance, such as that contained in the Chairman of the Joints Chiefs of Staff Manual and DoD Directives, has increased the risk that information assurance vulnerability alerts classified as critical remain unpatched.

4-1C. Cyber Security	Department Response

The Department continues to strengthen cyber security and address the threat posed by network attacks. The establishment of the U.S. Cyber Command and the supporting Service Component Commands has increased the Department's ability to plan, coordinate, integrate, synchronize, and conduct activities to lead the day-to-day defense and protection of DoD information networks. Implementing a Department-wide enterprise Host-based Security

System (HBSS), which includes a Host-based Intrusion Prevention (HIPS) module chosen in place of a host-based intrusion detection system to extend active protection to the desktop level, has been a key component of our defense-in-depth strategy as we take steps to effectively isolate the Department's official-use networks from the Internet while maintaining connectivity. This has been undertaken in phases, as we first focused on Secret network implementation and then unclassified networks. This implementation has been directed through U.S. Cyber command tasking and fragmentary orders.

Implementation of the HBSS HIPS module has been particularly challenging, as individual Components have had to adapt their HIPS implementation to work with the existing legacy information systems running on their networks. Some of these legacy systems are still vital for warfighting support. The U.S. Cyber Command and the supporting Component Commanders continue to focus on implementation, with Defense Information Systems Agency's assistance in providing program office and fielding support to ensure future versions of HBSS and HIPS software are modified, as necessary, to enable more rapid implementation.

In regard to the Department's challenges to recruit and retain cyber personnel, the U.S. Cyber Command is aggressively working through the manning process to fulfill established requirements in a time of shrinking budgets.

One of the focus areas of the DoD Chief Information Officer's (CIO's) 10-Point Plan for Information Technology (IT) Modernization is to strengthen IT investments. Section 804 of the NDAA for FY 2010 required the Secretary of Defense to develop and implement a new acquisition process for information systems. The process was to be based on recommendations from the March 2009 report of the Defense Science Board Task Force on Department of Defense Policies and Procedures for the Acquisition of Information Technology. This report concluded that "the conventional DoD acquisition process is too long and too cumbersome to fit the needs of the many systems that require continuous changes and upgrades…" The DoD CIO's 10-Point Plan includes structuring IT programs – via smaller, frequent deliveries – implementing an enterprise approach for the procurement of common IT hardware and software, obtaining transparency of IT investments with a full DoD IT investment portfolio, and reviewing major IT investments for performance, funding execution, and enterprise alignment.

4-2A. Cyber Workforce	IG Summary of Challenge

According to the National Initiative for Cyber Security Education, as the world grows more connected through cyberspace a highly skilled cyber security workforce is required to secure, protect, and defend our Nation's information systems. While the demand for cyber security professionals is high, the supply is low. For example, according to one leading research director, "Top notch cyber threat hunters and tool builders are in short supply. There are probably fewer than 800 of them in the entire country."

In the current environment of budget cuts, pay freezes, and furloughs, the Department faces a significant challenge in filling the multitude of cyber positions it needs to operate, defend, and protect its networks. In January 2013, it was reported that the Department planned to expand its cyber workforce five-fold, to transition from a mainly defensive force to one capable of a wide range of offensive operations. In addition, a June 2013 article on the Navy's U.S. Fleet Cyber Command reported that the Navy Cyber Command, in the next three years, will bring on nearly 1,000 cyber Service members. This is happening at a time when each of the other three Services' Cyber Commands is looking to increase the ranks of its own cyber workforce. In fact, the Government Accountability Office (GAO) issued its current *High Risk Series update in February 2013*, and strategic human capital management remains on the list of high risks. Specifically, GAO identified six Government-wide mission-critical occupations, one of which was information technology management/cyber security. Therefore, it is imperative that the Department develop the capability to recruit, train, and retain a cyber workforce in the competitive national environment.

4-2B. Cyber Workforce	IG Assessment of Progress

Growing and retaining a skilled cyber force is one of the biggest gaps in the cyberspace mission area. The Department has taken steps recently to build its cyber workforce. The DoD FY 2014 budget submission funds the re-organization of cyber forces into teams that will specialize in three functions: defending networks, degrading adversary cyber capabilities, and supporting defense of national infrastructure. The Department plans to assign more DoD civilians and contractors to this effort. In addition, the 2014 budget adds resources to increase the quality and throughput of DoD's training pipeline. Moreover, in June 2013, the Department coordinated a working draft of a DoD Cyberspace Workforce Strategy. The working draft contained the strategy for transforming DoD cyberspace workforce management and processes to recruit, train, and retain staff. Although the Department has made progress in the planning stages, it must maintain momentum through implementation.

4-2C. Cyber Workforce	**Department Response**

The Department is committed to developing a cyber workforce that is correctly sized and structured to secure, protect, and defend Department networks in the context of this ever-changing domain. This requires a comprehensive strategy for recruitment, training and retention that attracts skilled individuals and delivers training that is adaptable and responsive to evolving security threats. The Department plans to structure its cyber workforce in a way that provides both defensive and offensive capabilities.

The Department has developed a comprehensive strategy that outlines recruitment goals, reorganizes the cyber workforce, and incorporates tools for retention. This plan depends on adequate funding in FY 2014. The Department has developed a strategy providing for a phased cyber workforce development that is large enough and strategically structured to secure, protect, and defend Department networks. Budget constraints, including indiscriminate cuts, put that strategy at risk.

5. IG-Identified Challenge: Health Care

5-1A. Medical Readiness	IG Summary of Challenge

Medical readiness continues to be a challenge for the Department. Maintaining individual readiness for the Reserve Component is particularly challenging, because much of the responsibility for achieving individual medical readiness rests on the reservist. Reservists are responsible for maintaining individual medical readiness but are provided some help by the Department. Additionally, managing the overall health of 9.6 million eligible beneficiaries, which affects medical readiness, is a continuing challenge for the Military Health System (MHS). The MHS must identify unhealthy behaviors and provide interventions across the population. By reducing obesity and tobacco use, for example, the long-term health implications of diabetes and lung disease can be reduced significantly. Conditions such as these are expensive and long term in nature and could degrade medical readiness of military members.

5-1B. Medical Readiness	IG Assessment of Progress

According to a 2012 RAND Corporation report, the Department is making progress in raising Reserve Component individual readiness percentages. The Department's goal is to have 75 percent of Reservists fully medically ready. At the end of the second quarter of FY 2006, the Reserve Component reported that only 26 percent of its forces were fully medically ready. By the first quarter of FY 2010, 47 percent of Reserve Component forces were fully medically ready. According to the TRICARE Management Activity (TMA)[1], as of March 2013, 60 percent of the Reserve Component forces were fully medically ready. The Department should continue to emphasize improving individual medical readiness and strive to meet its 75 percent goal.

Additionally, the MHS management developed the family medical readiness strategic imperative, but its performance measure is in the concept phase. The MHS continues to implement the "medical home" concept throughout the direct-care system. With the medical home, the patient will have more direct access to a medical team equipped to recognize unhealthy behaviors and intervene early. In addition, line officers need to ensure nonmedical alternatives, such as recreational and athletic facilities, are in adequate condition and available to the military community.

Additionally, evidence-based community cessation programs for addictive behaviors should also be readily accessible. The MHS fully supports the National Prevention Strategy and the transition from a system of sick care to one based on wellness and prevention. One example of this commitment is the reduction in cigarette use among active duty forces from FY 2010 to FY 2011. The MHS has committed to supporting the National Partnership for Patients initiative with the Department of Health and Human Services to improve care, transition, and prevention of harm during treatment.

5-1C. Medical Readiness	**Department Response**

The Department concurs with the IG's assessment.

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[1] Effective October 1, 2013, the Department established the Defense Health Agency, which absorbed the functions of the TRICARE Management Activity and assumed responsibility for common clinical and business processes across the Military Health System.

5-2A. Cost Containment	IG Summary of Challenge

The MHS must provide quality care for 9.6 million beneficiaries within fiscal constraints and while facing increased user demand, legislative imperatives, and inflation. These factors make cost control difficult in the public and private sectors. Over the last decade, health-care costs have grown substantially, and MHS costs have been no exception. The DoD budget for health-care costs was $51 billion in FY 2013, an increase of 74 percent since FY 2005. The MHS costs have more than doubled, from $19 billion in FY 2001 to the Department's request of $49.4 billion for FY 2014. The FY 2013 amount does not include reductions due to sequestration.

Another challenge in containing health-care costs is fraud. Health-care fraud is among the top five categories of criminal investigations of the DoD IG's Defense Criminal Investigative Service, representing 15.7 percent of the 1,787 open cases at the beginning of FY 2013. Increasing health-care benefits also provides additional pressure to manage and contain costs.

5-2B. Cost Containment	IG Assessment of Progress

The Department's efforts in controlling health-care costs will continue to be a challenge. The MHS is focusing on many areas to manage per-capita health-care costs. Three managed-care support contracts are in effect; however, award protests resulted in staggered implementation of the new-generation TRICARE contracts. These contracts provide incentives for customer satisfaction and include managed-care support contractors as partners in support of medical readiness. The Department continues to examine how the MHS purchases health care from the private sector.

The Department has identified areas that assist in managing costs, including fraud management and prescription drugs. The managed-care support contracts have program-integrity units that review claims for indicators of fraud. We reported in December 2012 that these units met the requirements in their contracts. Specifically, the contractors:

- Submitted the required quarterly and annual reports;
- Implemented standard operating procedures for case development;
- Used anti-fraud software; submitted the minimum case referrals to TMA Program Integrity;
- Performed prepayment reviews; and
- Established mandatory fraud and abuse training.

The MHS has attempted to manage costs through increased use of the TRICARE Mail Order Pharmacy program. The TMA has implemented an aggressive communication plan to encourage the increased use of receiving prescription drugs through the mail to reduce costs.

The MHS Quadruple Aim Concept focuses on four factors in providing quality health care to DoD beneficiaries: readiness, population health, experience of care, and cost. Continuing to implement the MHS Quadruple Aim Concept should improve quality and reduce costs by focusing on improved care coordination and delivering care in the appropriate setting. Additionally, the MHS identified optimization of the pharmacy practices and implementation of the patient-centered medical home as strategic initiatives, both of which aim to increase the quality of health care while reducing its cost.

5-2C. Cost Containment	Department Response
The Department concurs with the IG's assessment.	

5-3A. Optimizing Health-Care Governance	IG Summary of Challenge

Ensuring that the MHS is organized in the most effective and cost-efficient manner is a major challenge. In March 2013, the Secretary of Defense directed the implementation of MHS reform. The centerpiece of this reform is the establishment of the Defense Health Agency (DHA) to assume responsibility for shared services, functions, and activities of the MHS and other common clinical and business processes. This new agency will operate as a Combat Support Agency and assumed many responsibilities of the TMA, which was disestablished on October 1, 2013. Over the next year, the MHS will face the challenge of transitioning to this new structure while continuing to execute the MHS mission. Additionally, the Secretary of Defense required the implementation of multi-Service market-management authorities for medical treatment facilities (MTFs) in six regions. The management authorities will:

- Manage the allocation of the budget for the market;
- Direct the adoption of common clinical and business functions;
- Optimize readiness to deploy medically ready forces and ready medical forces;
- Direct the movement of workload and workforce between or among the MTFs.

This joint approach to managing health care-related services in geographic markets will be especially challenging, considering that the MTFs in these markets have been managed individually to date by each of the Military Services. The MHS will also be challenged to standardize medical services across the Service Components.

5-3B. Optimizing Health-Care Governance	IG Assessment of Progress

Although the transition to the DHA and the implementation of the multi-Service market management authorities are in their infancy, the Department has made significant strides. The Department issued a draft DoD Directive for comment that establishes the DHA and the details of its mission, sets up the organizational structure, and delegates responsibilities and functions throughout the agency. The draft directive incorporated language consistent with the Secretary's requirement to implement multi-Service market-management authorities. In fact, the draft Directive states that the DHA, as part of its mission, supports coordinated management of the enhanced multi-Service market areas to create and sustain a cost-effective, coordinated, and high-quality health care system in those areas.

Additionally, the directive mandates that the DHA exercise control over the MTFs within the National Capital Region (one of the six market areas identified). The DHA reached its initial operating capability on October 1, 2013, and will achieve full operating capability within two years of the Secretary's memorandum. The Services' potential resistance to relinquishing control over managerial functions of their MTFs may be difficult to fully overcome. Lessons from prior shared-services models should help the Department with this transition.

5-3C. Optimizing Health-Care Governance	Department Response

The Department concurs with the IG's assessment.

5-4A. Rehabilitation and Transition Care	IG Summary of Challenge

The continued strengthening of comprehensive and integrated health care – from accession through active service, to rehabilitation, and when necessary, the transition of our wounded warriors to the Department of Veterans Affairs (VA) – is a major challenge for the MHS. Despite the drawdown in Southwest Asia, the Department must remain focused on providing adequate rehabilitation and transition care for wounded warriors. Key areas requiring management attention include rehabilitation and transition care for those with traumatic brain injuries or mental-health disorders and those in need of prosthetic devices. Access to mental-health care also remains a challenge. Suicide prevention, though not a specific MHS responsibility, confronts the MHS with the need to provide timely and thorough mental-health care for its beneficiaries.

Although the Department and the VA have identified objectives and initiated programs, the quality and oversight of these programs must be tightly managed. The Department should continue to strive to make the medical care and benefits transition program an efficient, transparent, and timely process, as wounded warriors move from the DoD system to the VA system.

5-4B. Rehabilitation and Transition Care	IG Assessment of Progress

During the last two years, DoD IG has noted the need for timely access to specialty care, improvements in training programs and plans, and improved medication management. Although challenges remain, DoD IG identified initiatives in the Department for supporting the comprehensive care, healing, and transition of wounded warriors. One initiative entailed recovery-team forums to develop individualized treatment for each wounded warrior. Another aimed to reduce the potential for exploitation of warriors, avoiding negative consequences to the overall health and welfare of the warriors. Wounded-warrior care centers were also developing meaningful programs of constructive activities to assist with warriors' transition. These notable initiatives should continue Department-wide.

5-4C. Rehabilitation and Transition Care	Department Response

The Department concurs with the IG's assessment.

6. IG-Identified Challenge: Equipping and Training Afghan National Security Forces

6-1A. Iraq Security Forces	IG Summary of Challenge

With the drawdown of U.S. combat forces from Iraq in 2011 and the establishment of normal diplomatic relations, equipping and training of the Iraq Security Forces no longer is considered to present a significant challenge for reporting. The United States is now represented in Iraq by the U.S. Ambassador, with the Department serving in a supporting role. The Office of Security Cooperation – Iraq (OSC-1), operating under Chief of Mission authority but administered by DoD personnel, is charged with performing vital bilateral security cooperation and security assistance functions. The OSC-1, comprised of DoD military, civilian, and contractor personnel, represents a cornerstone capability for building an enduring foundation for a long-term security relationship with the Government of Iraq.

6-2A. Afghan National Security Forces	IG Summary of Challenge

Between now and the end of 2014, the Department will continue to develop the Afghan National Security Force's (ANSF) capability to take ultimate responsibility for Afghanistan's security. Challenges include:

- Developing ministerial capability to plan and manage resources and human capital;
- Ensuring enabling-force capabilities are fielded prior to withdrawal of Coalition capabilities;
- Measuring and reporting ANSF operational readiness and effectiveness;
- Professionalizing the ANSF;
- Preparing for post-2014 operations.

Coalition force drawdown and retrograde, as well as securing Afghanistan's national elections in April 2014, will add additional challenges as ANSF completes the transition to full responsibility for security.

- **Security Ministries.** The Department must continue its focus on advising and assisting the development of the resource management capabilities of the Ministry of Interior and Ministry of Defense. Budget planning and execution, training and development of human resources, increasing the ranks of civilian professionals, and leader emphasis on command and control of logistics are key areas for continued emphasis. Additionally, coordination between the Afghan National Army (ANA), the Afghan National Police (ANP), and the Afghan Air Force (AAF) will be important to providing adequate support to the 2014 elections as well as to providing a multi-layered, long-term defense against insurgents and criminals.

- **Enabling Force Capabilities.** Completing the fielding of "enablers", or military capabilities essential to building ANSF's capacity to accomplish its missions, is increasingly important. Fielding and integration of combat and support capabilities in the ANA and ANP will remain a priority. As Coalition advisors and trainers are withdrawn, the Department must ensure that capability gaps do not occur. Additionally, the Department must continue to identify, assess, and address the advice, training, and assistance requirements for fielding enabling capabilities beyond 2014.

- **Assessment of ANSF Progress.** Assessing capabilities and capability gaps will become more difficult during Coalition force withdrawal. The Department's visibility of the operational readiness and effectiveness of ANSF units is diminishing as the numbers of

partners and advisors continue to decrease. The challenge is to ensure that sufficient skilled and qualified advisors are in key positions to continue assessing and developing ANSF leadership, command and control, and critical units.

- **Professionalization.** The Department must continue to support ANSF's current efforts to professionalize the force. Command reports show that recruitment and management of initial training at the enlisted and officer levels are becoming ANSF strengths. Developing quality leadership, managing sustainment and professional training, accurate training and personnel records, and providing career development opportunities, have all been identified as areas requiring continued efforts to develop and train professionals in the force.

- **Post-2014 Operations.** Although no decision has been made on the timing of when a transition of DoD's security cooperation and assistance activities to the Department of State will occur, the Department should begin planning for an eventual transition. The size, purpose, and support of Coalition forces and civilians remaining in Afghanistan in 2015 should be determined as soon as possible to facilitate planning and minimize risk of complications for this transition.

6-2B. Afghan National Security Forces	IG Assessment of Progress

Despite the current challenges in Afghanistan, much progress has been made. Most of the challenges above are recognized in Command reports as Coalition and ANSF priorities.

Since force levels are at over 95 percent of personnel end strength objective in both the ANA and ANP, and are approaching 90 percent of personnel end strength objectives in the AAF, the emphasis on ANSF development has shifted from force quantity, or growing the force, to force quality – sustaining and professionalizing the force.

Ministerial development is a primary emphasis, and the Coalition is increasing resource management training for security ministry personnel. Ministerial advisors are delivering assessments of the security ministry departments, reporting departmental setbacks as well as successes, and planning and revising training milestones and objectives as necessary.

With Coalition support, ANSF is committed to fielding a wide array of combat and combat support enablers that will provide ANSF the capability to operate independently and sustainably. Although ANSF logistics and force sustainment is still a primary concern as a force enabler, recent DoD IG assessments have noted some increased understanding and appreciation of the ANSF logistics system at the unit level.

Additionally, the shortage of human capital remains a challenge for ANSF; nevertheless, ANSF continues to support human capital development and training, particularly literacy training. The ANSF is scheduled to begin administering the literacy program by mid-2014.

The ANSF continues to take responsibility for its own training. Coalition reports confirm that the number of Afghan trainers has increased steadily over time, easing the burden on the Coalition Forces to provide military and civilian trainers between now and December 2014. Reportedly, ANSF is also managing its non-commissioned officer (NCO) and officer ranks more aggressively, for example, taking action to meet ANP non-commissioned officer (NCO) shortages by training and promoting qualified and experienced enlisted soldiers and junior NCOs.

Importantly, operational readiness and effectiveness of the ANA, measured by units rated "effective with advisors" or "independent with advisors," reportedly increases with each quarterly assessment. From October 2012 to March 2013, ANP ratings have become more static, and on-site tracking of the readiness and effectiveness of many ANP units has been discontinued due to the shortage of ANP advisors and partner units. To address this reporting

gap, the Coalition developed a second rating method in an effort to more accurately capture the readiness of ANSF units losing advisors or partners.

As of June 18, 2013, ANSF had assumed the lead for security nationwide, a significant milestone. Coalition forces have assumed a Train, Advise, and Assist rather than a combat role, except for force protection and certain counter-terrorism operations conducted with ANSF. As a consequence, Coalition casualties have significant reduced and those incurred by ANSF have commensurately increased. The Coalition is providing equipment to mitigate this trend to the extent possible, especially with respect to Improvised Explosive Device attacks, which account for many of the ANSF wounded or killed.

The Coalition is monitoring the performance of ANSF in the current fighting season to determine its strengths and weaknesses. According to the "Report on Progress Toward Security and Stability in Afghanistan", issued in July 2013 by the Secretary of Defense, Afghan forces generally have acquitted themselves well but will continue to face development challenges, including a number that will likely require continued support post-2014 to ensure they subsequently reach full independence and sustainability.

6-2C Afghan National Security Forces	Department Response
	The Department concurs with the IG's assessment.

7. IG-Identified Challenge: The Nuclear Enterprise

7-1A. Modernizing the Nuclear Force in the Face of Declining Resources	IG Summary of Challenge

Following the Soviet Union's collapse, the U.S. military began to shift from a nuclear centric "Cold War" posture, which had been the foundation of U.S. military strategy since the end of World War II. The new focus is to maintain a smaller, multi-purpose force which can address a larger spectrum of operations with the same weapon systems and personnel. With the start of the Overseas Contingency Operations following the attacks of September 11, 2001, greater focus has been placed on the military's ability to conduct limited armed conflicts and counter-insurgency operations.

During this transformation, each of the various defense programs was forced to redefine their capabilities and display how they meet this new paradigm. The key to a program's survival rests on its ability to validate its flexibility and capability to adapt to wide, multiple-mission roles. Weapon systems and defense programs displaying this capability were able to compete for funding during a time of shrinking budgets. All nuclear programs were perceived as a series of weapon systems rendered obsolete by current events. Those programs were also identified as being single-purpose systems that were inflexible and costly.

The nuclear infrastructure, delivery systems, manning, policies, and acquisition began to suffer. During a time when other countries modernized their nuclear forces, the budget was only sufficient to maintain a force that was 20 – 50 years old. Recently, the Services initiated modernization programs that, if funded, will lead to developing a modernized nuclear force within two decades.

Justifications for such improvements encounter scrutiny because of the basic nature of nuclear weapons and their use as a deterrent. Mandated budget sequestrations may affect current capabilities if age-related issues of the nuclear enterprise are not addressed.

7-1B. Modernizing the Nuclear Force in the Face of Declining Resources	IG Assessment of Progress

The Services have initiated several programs to transform the aging nuclear force into a modern nuclear deterrent arm capable of operating into the latter part of the 21st century. Renovating the nuclear enterprise comprises several programs that will sustain nuclear assets and develop replacement systems integrating the latest technologies. When completed in 2030, almost every component of the strategic nuclear force will be replaced or updated. However, federally-mandated budget cuts could threaten the upgrade and development of programs and extend the possible implementation dates or cancel completely some programs.

In an effort to accurately identify the critical command and control functions which are crucial in a nuclear crisis, the OSD Director of Cost Assessment and Program Evaluation developed a modeling simulation that maps the systems and flow of information used for force direction, force management, and adaptive planning of the nuclear forces. This tool allows planners and acquisition specialists to view the effectiveness of certain command and control systems in performing various tasks in the degraded communications environments expected during a nuclear attack. Using this tool, system users will be able to develop a strategy of how the command and control architecture operates and map out where vulnerabilities could exist and in defining acquisition priorities.

As part of the force modernization efforts to replace both the B-52 and B-2 bomber fleets, the Air Force has begun developmental steps to build the next generation of bombers, known as the Long Range Strike-Bomber. In 2013, senior Air Force officials reaffirmed that the 80 - 100 new bombers will be designed to meet their primary mission as a nuclear-delivery platform. However, the projected deployment date planned for the mid-2020s may be delayed due to the current budget situation.

As part of an on-going sustainment program, the B-2 bomber force is upgrading radar and nuclear command and control communications capabilities. The upgrades should extend for many years the service life of this bomber. Simultaneously, the B-52 fleet has been undergoing upgrades to global positioning systems, on-board computers, and an expansion to the variety of weapons the bomber can carry. These upgrades will ensure that the fleet is viable until the new bomber is operational.

The Air Launched Cruise Missile is the main-stay weapon for the B-52 fleet and allows the crews to strike targets well outside an adversary's defense system. As missile stockpiles age and decline in number, the Air Force is studying various options to replace the current cruise missile fleet. If no delays are encountered, the Air Force estimates a production start in 2025.

The Minuteman III Intercontinental Ballistic Missile (ICBM) fleet was originally fielded in the mid-1970s and has been undergoing several upgrades and corrective maintenance actions. The ICBM Modernization and Replacement Program, the most current of these enhancement plans, will extend the operational life of the ICBMs through 2020 and possibly to 2040. This program modernizes the missile's guidance control and targeting systems and changes the rocket motor propellants.

In FY 2012, the Air Force initiated a two-year study to replace the Minuteman ICBM system. The project will examine the essential capabilities and future technologies that could be available to incorporate into the design of the next generation ICBM. The Air Force will decide the acquisition path at the completion of the study.

The Navy continues developing a follow-on ballistic missile submarine to replace the current 30-year-old Ohio class submarine fleet. Under the management of the Strategic Systems Program office, the Ohio Replacement Program was formed to research and design the next-generation strategic deterrence submarine. This program will deploy 12 submarines, beginning with the lead ship of the class being delivered in 2028, near the projected decommission date for the first of the Ohio class strategic missile boats.

Similar to the Minuteman Ill upgrade program, the Navy has begun carrying out a project to modernize the Trident II sea-launched ballistic missile. This sustainment upgrade is projected to extend the missile's operational life through 2030. Pre-sequester cost reductions have delayed a Trident replacement until at least 2029.

As the Services have initiated a full-scale rejuvenation of all three legs of the nuclear triad, they must balance the various programs against an ever-tightening budget if the nuclear enterprise is to fully benefit from this rejuvenation.

7-1C. Modernizing the Nuclear Force in the Face of Declining Resources	Department Response

The Department continues progress with its nuclear weapon systems and platform modernization programs, despite federally mandated budget cuts. The Department is working closely with the National Nuclear Security Administration to address future program gaps. With this modernization effort, the Department is actively sustaining and upgrading existing nuclear forces, ensuring a viable nuclear deterrent until follow-on weapon systems are implemented.

Although faced with significant fiscal challenges, the Department has issued clear guidance that the Nuclear Enterprise is of the highest priority and, as a result, funding levels will be maintained. Progress has been made in improving the morale and proficiency of personnel within the nuclear enterprise, but challenges remain in light of budget cuts and the uncertainty of the career field amidst potential arms control reductions. At the same time, a robust inspection program continues to ensure the highest of standards of performance are maintained. The focused efforts of the Department and the interagency team maintain a safe, secure, and effective nuclear deterrent. The Department will continue to work with the interagency to address the challenges and opportunities presented in this report to maintain a well-managed and efficient nuclear enterprise.

7-2A. Redefining the Importance of the Nuclear Enterprise and Overcoming Past Neglect	IG Summary of Challenge

Several high-profile incidents over the past 10 years highlight the lack of emphasis on the nuclear enterprise. Recent news reports regarding morale and proficiency problems at one of the three Air Force Missile Bases will only continue to make the general public question the nuclear deterrent mission's reliability.

Reestablishing the enterprise's importance and performance will take time, funding, and a fundamental change in attitude by everyone associated with the nuclear weapons community. The nuclear enterprise will face additional challenges to complete this transformation due to mandated funding cuts. These reductions will also negatively affect maintaining the proficiency required for managing the nuclear force.

7-2B. Redefining the Importance of the Nuclear Enterprise and Overcoming Past Neglect	IG Assessment of Progress

While the decline or even the perception of such neglect cannot be corrected overnight, the revamped nuclear enterprise is making headway to address the key problems. The most significant challenge that the enterprise faces is to maintain the nuclear communities' current systems at the highest level of mission capability while meeting public expectations of flawless operations. This must be done despite budget cuts resulting from the government-directed sequester.

The efforts and challenges facing the nuclear community:

DoD. The Deputy Secretary of Defense directed the Defense Information System Agency to stand up an organization to address end-to-end system engineering in the enterprise. This new group will also bridge the nuclear command, control, and communications with the various critical systems that support continuity of government and operations, and presidential/senior leadership communications, in a crisis.

Joint Staff. As the focal point for the oversight of the nuclear enterprise, the Joint Staff's Deputy Directorate for Nuclear Command and Control continues to assess the capabilities of the nuclear command, control and communications systems necessary to ensure both the safeguarding and viability of the nuclear deterrent mission.

- To improve the procedures used for nuclear command and control orders, the Joint Staff has comprehensively evaluated the nuclear command and control guidance and processes it issues to the enterprise. The evaluation was done to ensure that the guidance and doctrines derived from the Joint Staff documents streamline systems' operational capabilities while maintaining the needed nuclear safeguards.

- The Joint Staff continues to expand on the fidelity of its Staff/Command Assistance Visit program. This program measures the level of proficiency with which combatant command centers and certain military nuclear command and control platforms provide the President with control of nuclear forces in a time of crisis. Under a 2012 initiative, the scope of the Joint Staff assessments has expanded to ensure that the evaluations provide a more detailed assessment of the personnel and capabilities of the command locations. These details are provided by presenting more in-depth testing and scenario evaluations to judge operator knowledge and performance of the different systems.

- The Joint Staff is also continuing programs that evaluate the systems used in both the command and control of the nuclear enterprise, the transmission and reception of nuclear control orders. Detailed scenario tests have continued despite federally-mandated budget constraints. The operating constraints thrust on participating units, caused by additional budget reductions, may affect the effectiveness of future assessments.

Navy. Navy E-6 units that support the communications networks will continue to meet their nuclear support requirements, but these units expect the loss of flight hours to affect crew training. While reduced training hours will affect the enterprise's flying component, the budget cuts will not affect the Submarine Ballistic Missile fleet.

Air Force. Despite the mandated sequestrations, the Air Force has given priority to funding the nuclear deterrence mission. However, combat air forces supporting the nuclear mission may be affected if funding is depleted before the end of the fiscal year.

- The Air Force has been forced to reduce the depot level maintenance and engine service sustainment programs for the B-52 and KC-135 fleet. Even with giving priority to the nuclear mission, the Air Force's 18 percent reduction in flight hours will affect the manned bomber force's training proficiency.

- Since its creation in August 2009, Air Force Global Strike Command has brought the Air Force deterrent mission together under one command. However, a 2013 DoD IG audit found that the Air Force Headquarters staff is still struggling to decide where managing some of its nuclear responsibility actually rests. One example identified in a recent IG report found that the nuclear command, control, and communications systems management was alternating between the nuclear directorate. Another example involves stove-piping nuclear communications systems within one command, while another command is responsible for managing overall cyber and cryptographic upgrades.

- The DoD IG examined the Response Task Force program's ability to effectively react to weapon incidents and found that it had made great progress in this area. However, the Department needs to better define the requirements and readiness levels required for the Response Task Forces.

The Military Services continue to emphasize the physical security programs supporting the nuclear forces. The DoD IG will continue to monitor-long term improvements, such as the Air Force's work to field a replacement for the UH-1 "Huey" helicopter.

An Associated Press article about 19 Intercontinental Ballistic Missile crewmembers at Minot Air Force Base, North Dakota, being relieved from missile duty could be negatively perceived by the general public. However, the actions mentioned in the article resulted from proactive leadership trying to ensure that the highest levels of competency exist in the U.S. nuclear force. The Air Force has acknowledged the challenge to improve sagging morale that was identified from this incident. Senior Air Force leaders have acknowledged that morale problems at Minot stem from missile crew members' perception of a lack of communication from higher headquarters about the future of the nuclear force and the crews' concerns that they lack career advancement and diverse assignments. As part of this corrective action, the Air Force will need to address how it will manage nuclear-related career fields to ensure the enterprise has the necessary expertise and leadership through enrichment opportunities and advancement. The Chairman of the Joint Chiefs of Staff personally acted to show that senior

leadership was concerned about this issue by visiting Minot in mid-June 2013. He told the troops in an hour-long address that, "As far as I'm concerned, we can't pay you enough for what you do for our country." This message to the troops will greatly help if meaningful actions follow to establish challenging career paths.

In response to these problems, national leadership has directed studies to address the causes of missile force deterioration. Once these studies are completed, a course of action will be created to return both the credibility and surety that is essential to maintain an effective deterrence force.

7-2C. Redefining the Importance of the Nuclear Enterprise and Overcoming Past Neglect	Department Response

The Department continues progress with its nuclear weapon systems and platform modernization programs, while maintaining close collaboration with the interagency team to make difficult choices in light of fiscal austerity and federally mandated budget cuts. The Department is also working closely with the National Nuclear Security Administration to address future capability gaps. Concurrent with this modernization effort, the Department is actively sustaining and upgrading existing nuclear forces, ensuring a viable nuclear deterrent until follow-on weapon systems are fielded.

Although faced with significant fiscal challenges, the Department has issued clear guidance that the Nuclear Enterprise is of the highest priority and funding levels will be maintained. Progress has been made in improving the morale and proficiency of personnel within the nuclear enterprise, but challenges remain in light of current fiscal challenges and the uncertainty of the career field with regards to potential future arms control reductions. At the same time, a robust inspection program continues to ensure the highest of standards of performance are maintained. The focused efforts of the Department and the interagency team maintain a safe, secure, and effective nuclear deterrent. The Department will continue to work with the interagency to address the challenges and opportunities presented in this report to maintain a well-managed and efficient nuclear enterprise.