THE FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT OF 1996: ARE AGENCIES MEETING THE CHALLENGE?

HEARING

BEFORE THE

SUBCOMMITTEE ON GOVERNMENT EFFICIENCY, FINANCIAL MANAGEMENT AND INTERGOVERNMENTAL RELATIONS

OF THE

COMMITTEE ON GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

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THE FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT OF 1996: ARE AGENCIES MEETING THE CHALLENGE?

THURSDAY, JUNE 6, 2002

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON GOVERNMENT EFFICIENCY, FINANCIAL MANAGEMENT AND INTERGOVERNMENTAL RELATIONS,
COMMITTEE ON GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 10 a.m., in room 2247, Rayburn House Office Building, Hon. Stephen Horn (chairman of the subcommittee) presiding.

Present: Representative Horn.

Staff present: J. Russell George, staff director and chief counsel; Bonnie Heald, deputy staff director; Henry Wray, senior counsel; Rosa Harris, GAO detailee; Justin Paulhamus, clerk; Chris Barkley, new subcommittee staff; Michael Sazonov and Sterling Bentley, interns; David McMillen, minority professional staff member; and Jean Gosa, minority clerk.

Mr. HORN. A quorum being present, the Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations will come to order. I thank the panel for appearing. And if you'll stand and raise your right hand, and if you have any assistants behind you that will be also talking, the clerk will take all of the names for the record.

[Witnesses sworn.]

Mr. HORN. The clerk will note that the oath has been taken.

The Federal Financial Management Improvement Act requires the 24 major departments and agencies in the executive branch to have systems that can produce timely, reliable, and useful information for managing their day-to-day operations.

[The information referred to follows:]

FUNDS APPROPRIATED TO THE PRESIDENT

FEDERAL DRUG CONTROL PROGRAMS

SPECIAL FORFEITURE FUND

(INCLUDING TRANSFER OF FUNDS)

For activities authorized by Public Law 100–690, as amended, $112,900,000, of which $42,000,000 shall be transferred to the United States Customs Service for the conversion of one P–3AEW aircraft for the air interdiction program; of which $10,000,000 shall be available for transfer to other Federal agencies for methamphetamine reduction efforts; and of which $60,900,000 shall be available to the Director of the Office of National Drug Control Policy for enhancing other drug control activities, including transfer to other Federal agencies: *Provided*, That of the amount provided, $112,900,000 is designated by Congress as an emergency requirement pursuant to section 251(b)(2)(D)(i) of the Balanced Budget and Emergency Deficit Control Act of 1985, as amended to become available only upon receipt by the Congress of a supplemental request from the President requesting such designation.

Federal Financial Management Improvement Act of 1996. 31 USC 3512 note.

TITLE VIII—FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT

SEC. 801. SHORT TITLE

This title may be cited as the "Federal Financial Management Improvement Act of 1996."

31 USC 3512 note.

SEC. 802. FINDINGS AND PURPOSES.

(a) FINDINGS.—The Congress finds the following:

(1) Much effort has been devoted to strengthening Federal internal accounting controls in the past. Although progress has been made in recent years, Federal accounting standards have not been uniformly implemented in financial management systems for agencies.

(2) Federal financial management continues to be seriously deficient, and Federal financial management and fiscal practices have failed to—

(A) identify costs fully;

(B) reflect the total liabilities of congressional actions; and

(C) accurately report the financial condition of the Federal Government.

(3) Current Federal accounting practices do not accurately report financial results of the Federal Government or the full costs of programs and activities. The continued use of these practices undermines the Government's ability to provide credible and reliable financial data and encourages already widespread Government waste, and will not assist in achieving a balanced budget.

(4) Waste and inefficiency in the Federal Government undermine the confidence of the American people in the government and reduce the federal Government's ability to address vital public needs adequately.

(5) To rebuild the accountability and credibility of the Federal Government, and restore public confidence in the Federal

Government, agencies must incorporate accounting standards and reporting objectives established for the Federal Government into their financial management systems so that all the assets and liabilities, revenues, and expenditures or expenses, and the full costs of programs and activities of the Federal Government can be consistently and accurately recorded, monitored, and uniformly reported throughout the Federal Government.

(6) Since its establishment in October 1990, the Federal Accounting Standards Advisory Board (hereinafter referred to as the "FASAB") has made substantial progress toward developing and recommending a comprehensive set of accounting concepts and standards for the Federal Government. When the accounting concepts and standards developed by FASAB are incorporated into Federal financial management systems, agencies will be able to provide cost and financial information that will assist the Congress and financial managers to evaluate the cost and performance of Federal programs and activities, and will therefore provide important information that has been lacking, but is needed for improved decision making by financial managers and the Congress.

(7) The development of financial management systems with the capacity to support these standards and concepts will, over the long term, improve Federal financial management.

(b) PURPOSE—The purposes of this Act are to—

(1) provide for consistency of accounting by an agency from one fiscal year to the next, and uniform accounting standards throughout the Federal Government;

(2) require Federal financial management systems to support full disclosure of Federal financial data, including the full costs of Federal programs and activities, to the citizens, the Congress, the President, and agency management, so that programs and activities can be considered based on their full costs and merits;

(3) increase the accountability and credibility of federal financial management;

(4) improve performance, productivity and efficiency of Federal Government financial management;

(5) establish financial management systems to support controlling the cost of Federal Government;

(6) build upon and complement the Chief Financial Officers Act of 1990 (Public Law 101–576; 104 Stat 2838), the Government Performance and Results Act of 1993 (Public Law 103–62 107 Stat. 285) and the Government Management Reform Act of 1994 (Public Law 103–356; 108 Stat. 3410); and

(7) increase the capability of agencies to monitor execution of the budget by more readily permitting reports that compare spending of resources to results of activities.

SEC. 803. IMPLEMENTATION OF FEDERAL FINANCIAL MANAGEMENT IMPROVEMENTS. 31 USC 3512 note.

(a) IN GENERAL.—Each agency shall implement and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the United States Government Standard General Ledger at the transaction level.

(b) AUDIT COMPLIANCE FINDING.—

(1) IN GENERAL.—Each audit required by section 3521(e) of title 31, United States Code, shall report whether the agency financial management systems comply with the requirements of subsection (a).

(2) CONTENT OF REPORTS.—When the person performing the audit required by section 3521(e) of title 31, United States Code, reports that the agency financial management systems do not comply with the requirements of subsection (a), the person performing the audit shall include in the report on the audit—

(A) the entity or organization responsible for the financial management systems that have been found not to comply with the requirements of subsection (a);

(B) all facts pertaining to the failure to comply with the requirements of subsection (a), including—

(i) the nature and extent of the noncompliance including areas in which there is substantial but not full compliance;

(ii) the primary reason or cause of the noncompliance;

(iii) the entity or organization responsible for the non-compliance; and

(iv) any relevant comments from any responsible officer or employee; and

(C) a statement with respect to the recommended remedial actions and the time frames to implement such actions.

(c) COMPLIANCE IMPLEMENTATION.—

(1) DETERMINATION.—No later than the date described under paragraph (2), the Head of an agency shall determine whether the financial management systems of the agency comply with the requirements of subsection (a). Such determination shall be based on—

(A) a review of the report on the applicable agency-wide audited financial statement;

(B) any other information the Head of the agency considers relevant and appropriate.

(2) DATE OF DETERMINATION.—The determination under paragraph (1) shall be made no later than 120 days after the earlier of—

(A) the date of the receipt of an agency-wide audited financial statement; or

(B) the last day of the fiscal year following the year covered by such statement.

(3) REMEDIATION PLAN.—

(A) If the Head of an agency determines that the agency's financial management systems do not comply with the requirements of subsection (a), the head of the agency, in consultation with the Director, shall establish a remediation plan that shall include resources, remedies, and intermediate target dates necessary to bring the agency's financial management systems into substantial compliance.

(B) If the determination of the head of the agency differs from the audit compliance findings required in subsection (b), the Director shall review such determinations and provide a report on the findings to the appropriate committees of the Congress.

(4) TIME PERIOD FOR COMPLIANCE.—A remediation plan shall bring the agency's financial management systems into substantial compliance no later than 3 years after the date a determination is made under paragraph (1), unless the agency, with concurrence of the Director—

(A) determines that the agency's financial management systems cannot comply with the requirements of subsection (a) within 3 years;

(B) specifies the most feasible date for bringing the agency's financial management systems into compliance with the requirements of subsection (a); and

(C) designates an official of the agency who shall be responsible for bringing the agency's financial management systems into compliance with the requirements of subsection (a) by the date specified under subparagraph (B).

SEC. 804. REPORTING REQUIREMENTS.

31 USC 3512 note.

(a) REPORTS BY THE DIRECTOR.—No later than March 31 of each year, the Director shall submit a report to the Congress regarding implementation of this Act. The Director may include the report in the financial management status report and the 5-year financial management plan submitted under section 3512(a)(1) of title 31, United States Code.

(b) REPORTS BY THE INSPECTOR GENERAL.—Each Inspector General who prepares a report under section 5(a) of the Inspector General Act of 1978 (5 U.S.C. App.) shall report to Congress instances and reasons when an agency has not met the intermediate target dates established in the remediation plan required under section 3(c). Specifically the report shall include—

(1) the entity or organization responsible for the non-compliance;

(2) the facts pertaining to the failure to comply with the requirements of subsection (a), including the nature and extent of the non-compliance, the primary reason or cause for the failure to comply, and any extenuating circumstances; and

(3) a statement of the remedial actions needed to comply.

(c) REPORTS BY THE COMPTROLLER GENERAL.—No later than October 1, 1997, and October 1, of each year thereafter, the Comptroller General of the United States shall report to the appropriate committees of the Congress concerning—

(1) compliance with the requirements of section 3(a) of this Act, including whether the financial statements of the Federal Government have been prepared in accordance with applicable accounting standards; and

(2) the adequacy of applicable accounting standards for the Federal Government.

SEC. 805. CONFORMING AMENDMENTS.

31 USC 3512 note.

(a) AUDITS BY AGENCIES.—Section 3521(f)(1) of title 31, United States Code, is amended in the first sentence by inserting "and the Controller of the Office of Federal Financial Management" before the period.

(b) FINANCIAL MANAGEMENT STATUS REPORT.—Section 3512(a)(2) of title 31, United States Code, is amended by—

(1) in subparagraph (D) by striking "and' after the semicolon;

(2) by redesignating subparagraph (E) as subparagraph (F); and

(3) by inserting after subparagraph (D) the following:

"(E) a listing of agencies whose financial management systems do not comply substantially with the requirements of Section 3(a) the Federal Financial Management Improvement Act of 1996, and a summary statement of the efforts underway to remedy the noncompliance; and"

(c) INSPECTOR GENERAL ACT OF 1978.—Section 5(a) of the Inspector General Act of 1978 is amended—

5 USC app.

(1) in paragraph (11) by striking "and" after the semicolon;

(2) in paragraph (12) by striking the period and inserting "; and"; and

(3) by adding at the end the following new paragraph: "(13) the information described under section 05(b) of the Federal Financial Management Improvement Act of 1996."

31 USC 3512 note.

SEC. 806. DEFINITIONS.

For purposes of this title:

(1) AGENCY.—The term "agency" means a department or agency of the United States Government as defined in section 901(b) of title 31, United States Code.

(2) DIRECTOR.—The term "Director" means the Director of the Office of Management and Budget.

(3) FEDERAL ACCOUNTING STANDARDS.—The term "Federal accounting standards" means applicable accounting principles, standards, and requirements consistent with section 902(a)(3)(A) of title 31, United States Code.

(4) FINANCIAL MANAGEMENT SYSTEMS.—The term "financial management systems" includes the financial systems and the financial portions of mixed systems necessary to support financial management, including automated and manual processes, procedures, controls, data, hardware, software, and support personnel dedicated to the operation and maintenance of system functions.

(5) FINANCIAL SYSTEM.—The term "financial system" includes an information system, comprised of one or more applications, that is used for—

(A) collecting, processing, maintaining, transmitting, or reporting data about financial events;

(B) supporting financial planning or budgeting activities;

(C) accumulating and reporting costs information; or

(D) supporting the preparation of financial statements.

(6) MIXED SYSTEM.—The term "mixed system' means an information system that supports both financial and nonfinancial functions of the Federal Government or components thereof.

31 USC 3512 note.

SEC. 807. EFFECTIVE DATE.

This title shall take effect for the fiscal year ending September 30, 1997.

SEC. 808. REVISION OF SHORT TITLES.—

(a) Section 4001 of Public Law 104–106 (110 Stat. 642; 41 U.S.C. 251 note) is amended to read as follows:

"SEC. 4001. SHORT TITLE.

"This division and division E may be cited as the 'Clinger-Cohen Act of 1996'.".

(b) Section 5001 of Public Law 104–106 (110 Stat. 679; 40 U.S.C. 1401 note) is amended to read as follows:

"SEC. 5001. SHORT TITLE.

"This division and division D may be cited as the 'Clinger-Cohen Act of 1996'.".

(c) Any reference in any law, regulation, document, record, or other paper of the United States to the Federal Acquisition Reform Act of 1996 or to the Information Technology Management Reform Act of 1996 shall be considered to be a reference to the Clinger-Cohen Act of 1996.

This Act may be cited as the "Treasury, Postal Service, and General Government Appropriations Act, 1997".

TITLE II—ECONOMIC GROWTH AND REGULATORY PAPERWORK REDUCTION

Economic Growth and Regulatory Paperwork Reduction Act of 1996.
12 USC 226 note.

SEC. 2001. SHORT TITLE; TABLE OF CONTENTS; DEFINITIONS

(a) SHORT TITLE.—This title may be cited as the "Economic Growth and Regulatory Paperwork Reduction Act of 1996".

(b) TABLE OF CONTENTS.—The table of contents for this title is as follows:

TITLE II—ECONOMIC GROWTH AND REGULATORY PAPERWORK REDUCTION

Mr. HORN. The act requires the agencies to implement and maintain financial systems that comply with: Federal financial management system requirements; applicable Federal accounting standards; and the U.S. Government Standard General Ledger.

It has been nearly 6 years since the act became law. Yet, most agencies still do not comply with these three basic accounting requirements. In fiscal year 2001, 20 of the 24 major departments and agencies failed to comply with the act, compared to fiscal year 2000 in which 19 agencies failed to comply.

During the July 9th subcommittee hearing, the Comptroller General of the United States, Mr. David Walker, noted that "Noncompliance with the Federal Financial Management Improvement Act is indicative of the overall continuing poor condition of many financial management systems across government."

We recognize that there are long-standing problems with agency financial management systems. We also recognize that correcting these deficiencies will take time. However, the requirements of this act must be taken seriously, and I don't think they have been.

Today, we will discuss the challenges that are preventing many agencies from having financial management systems that comply with the act. The basic accounting requirements found in the Federal Financial Management Improvement Act can, and must, be achieved. American taxpayers deserve no less from their government.

[The prepared statement of Hon. Stephen Horn follows:]

ONE HUNDRED SIXTH CONGRESS

Congress of the United States

House of Representatives

COMMITTEE ON GOVERNMENT REFORM

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Opening Statement
Chairman Stephen Horn, R-CA
Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations
June 6, 2002

A quorum being present, the Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations will come to order.

The Federal Financial Management Improvement Act requires the 24 major departments and agencies in the executive branch to have systems that can produce timely, reliable, and useful information for managing their day-to-day operations.

The Act requires the agencies to implement and maintain financial systems that comply with:

- Federal financial management system requirements;
- Applicable Federal accounting standards; and
- The U.S. Government Standard General Ledger.

It has been nearly six years since this Act became law. Yet, most agencies still do not comply with these three basic accounting requirements. In fiscal year 2001, 20 of the 24 major departments and agencies failed to comply with the Act compared to fiscal year 2000 in which 19 agencies failed to comply.

During an April 9th hearing before this subcommittee, the Comptroller General of the United States said, "... noncompliance with the Federal Financial Management Improvement Act is indicative of the overall continuing poor condition of many financial management systems across government."

We recognize that there are long-standing problems with agency financial management systems. We also recognize that correcting these deficiencies will take time. However, the requirements of this Act must be taken seriously.

Today, we will discuss the challenges that are preventing many agencies from having financial management systems that comply with the Act. The basic accounting requirements found in the Federal Financial Management Improvement Act can -- and must -- be achieved. American taxpayers deserve no less from their government.

We welcome each of our witnesses today, and look forward to their testimony.

Mr. HORN. We welcome each of our witnesses today and look forward to your testimony to see why things are not happening the way they should be happening. We will begin with Sally Thompson, the Director of Financial Management and Assurance, U.S. General Accounting Office. She reports to the Comptroller General of the United States.

Ms. Thompson.

STATEMENT OF SALLY E. THOMPSON, DIRECTOR, ACCOMPANIED BY THOMAS R. BRODERICK, ASSISTANT DIRECTOR, FINANCIAL MANAGEMENT AND ASSURANCE, U.S. GENERAL ACCOUNTING OFFICE

Ms. THOMPSON. Thank you, Mr. Chairman. And I'm very pleased to be here today to discuss with you and the other members of the committee, if they come in, the challenges that most of the Federal departments and agencies are still facing in meeting the basic expectations outlined in the Federal Financial Management Improvement Act of 1996. Many of those you just mentioned.

The primary purpose of FFMIA is to ensure that agency financial management systems routinely—and I stress "routinely"—produce reliable, accurate, timely data for management decisionmaking. Government leaders will be in a better position to invest resources, reduce costs, oversee programs and, importantly, hold agency managers accountable for the way they manage programs.

I would like to emphasize this morning that FFMIA is not a compliance issue; it's a management tool. And getting a clean opinion does not mean that people have a management tool and comply with FFMIA. We certainly have seen that to be the case when, over the last 5 years, we still only have four Federal agencies whose IGs say that they are compliant in FFMIA, and yet we have 18 clean opinions and that has been increasing from about 13, 5 years ago. So we're continuing to get clean opinions, but we're not getting success in FFMIA.

This decrease also means that agencies have been able to achieve these clean opinions, first of all, 5 months after year-end, but with an enormous amount of resources, as we see in the horrendous numbers of adjustments made. Whenever you make adjustments to numbers at the year-end or 5 months after year-end, that means that you didn't have information on a daily basis on which to make management decisions.

We need to take FFMIA information from the back room and into the board room where management decisions are being made. What I mean by this is getting a management tool with management information is not just a CFO issue, it is more than an accounting issue. It's not a CIO issue, which would be hardware/software, but it is a combination of the CIO, the CFO, and the program managers working together.

It also includes integrating budget information with program information with performance results and accounting, and coming up with what we call cost management information for decisionmaking.

This would provide the information that we need, that program managers need to make allocation of resources and need to be able to determine the outcomes of their programs.

I look at systems as being much broader than just hardware/software. I look at it including the business processes and procedures and controls and the type of information that's needed to be able to assess whether programs are meeting these intended results and outcomes.

It will take a committed involvement from the Secretary's level all the way down to achieve success in FFMIA. It's a multidisciplinary process of tackling systems modernization in order to reach the success. And again I would say that it would include the chief operating officer that could spearhead this, but it would include the CFO, the CIO, the budget officer and, most importantly, program managers. These officials are best positioned to determine what kind of information needs to be captured in order to be able to measure the outcomes and ensure the results by again combining accounting, budget and program systems integrated together.

Probably one of the key elements of success in FFMIA is capturing what we're calling the cost management information. It is critical to transforming how government manages the business of government.

We have several ongoing assignments in agencies that we hope will result in executive guidance. What we found was a real lack of guidance out there on how do you get to good cost management information. Again, we have seen, and you've probably heard a lot about, activity-based costing and now a new term, activity-based budgeting. I would say, combining that with activity-based performance, all three of those together, will get you cost management information.

The President's Management Agenda has five areas that they're looking at, which includes human capital, competitive resources, e-government, and budget and performance integration and also improved financial management. I would say to you that the implementation of FFMIA is the solid foundation to be able to get that kind of information together. In other words, you cannot achieve any of the five of the President's Management Agenda items without a solid financial system. FFMIA success in systems and standards, and the policy area depend on this. If we look at the problems, they've been long and they haven't really changed over the last 5 years. And I'd be glad to answer any questions.

[The prepared statement of Ms. Thompson follows:]

United States General Accounting Office

GAO

Testimony
Before the Subcommittee on Government Efficiency, Financial Management and Intergovernmental Relations, Committee on Government Reform, House of Representatives

For Release on Delivery
Expected at 10 a.m. EDT
Thursday,
June 6, 2002

FINANCIAL MANAGEMENT

Effective Implementation of FFMIA Is Key to Providing Reliable, Useful, and Timely Data

Statement of Sally E. Thompson
Director, Financial Management and Assurance

GAO
Accountability * Integrity * Reliability

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here to discuss the challenges most of the federal departments and agencies still face in meeting the basic expectations outlined in the Federal Financial Management Improvement Act (FFMIA). As you requested, our testimony today addresses the status of agencies' efforts to implement and maintain systems that substantially comply with FFMIA.

FFMIA builds on the foundation laid by the Chief Financial Officers (CFO) Act of 1990 by emphasizing the need for agencies to have financial management systems that can generate timely, accurate, and useful information with which to make informed decisions and to ensure accountability on an ongoing basis. FFMIA requires the 24 CFO Act agencies to implement and maintain financial management systems that comply substantially with the (1) federal financial management systems requirements, (2) applicable federal accounting standards, and (3) *U.S. Standard General Ledger* (SGL) at the transaction level. Further, FFMIA requires auditors to report in their CFO Act financial statement audit reports whether the agencies' financial management systems comply with FFMIA's requirements. We are also required to report annually on the implementation of the act. We plan to issue our sixth annual report on agency compliance with FFMIA by October 1 of this year.

The results of the fiscal year 2001 FFMIA assessments performed by agency inspectors general (IG) or their contract auditors again show that the same types of problems still plague the financial management systems used by the 24 CFO Act agencies. While much more severe at some agencies than others, the nature and severity of the problems indicate that, overall, agency management lacks the full range of information needed for accountability, performance reporting, and decision making. While the CFO Act agencies have obtained more clean or unqualified audit opinions on their financial statements, often through extraordinary, labor-intensive measures, there is little evidence of marked improvements in agencies' capacities to create the full range of information needed to manage day-to-day operations. As we have previously testified[1] before this subcommittee,

[1] U.S. General Accounting Office, *U.S. Government Financial Statements: FY 2001 Results Highlight the Continuing Need to Accelerate Federal Financial Management Reform*, GAO-02-599T (Washington, D.C.: April 9, 2002) and *Financial Management: Agencies Face Many Challenges in Meeting the Goals of the Federal Financial Management Improvement Act*, GAO/T-AIMD-00-178 (Washington, D.C.: June 6, 2000).

if agencies continue year after year to rely on significant costly and time-intensive manual efforts to achieve or maintain unqualified opinions without improving underlying financial management systems, it can mislead the public about the true status of the agencies' financial management capabilities. An unqualified opinion achieved on this basis will become an accomplishment without much substance.

Increasing attention from the highest levels of the federal government is being targeted on improving federal financial management. Most importantly, *The President's Management Agenda Fiscal Year 2002* includes improved financial performance as one of the five top governmentwide management goals. Improvement in federal financial management systems is central to achieving improved financial performance. The administration plans to use the Executive Branch Management Scorecard to highlight agency progress in achieving the management and performance improvements embodied in the *President's Management Agenda*. Moreover, the Joint Financial Management Improvement Program (JFMIP) principals[2] have been holding a series of periodic meetings that have resulted in unprecedented substantive deliberations and agreements focused on key reform issues such as better-defined measures for gauging financial management success and the establishment of audit committees. In addition, the JFMIP principals have agreed to significantly accelerate financial statement reporting so that the government's financial statements are more timely and to discourage costly efforts designed to obtain unqualified opinions without addressing underlying systems challenges. For fiscal year 2004, agency audited financial statements are to be issued no later than November 15. These top management efforts underscore the critical need for the modernization of financial management systems as called for by the CFO Act, including the systematic measurement of performance; development of cost information; and integration of program, budget, and financial information.

Today I will discuss (1) auditors' determinations of FFMIA compliance for fiscal year 2001, (2) problems that affect agency systems' compliance with FFMIA, (3) current actions leading to renewed emphasis on timely, accurate, and useful information from federal financial management

[2]The JFMIP principals are the Secretary of the Treasury, the Directors of the Office of Management and Budget (OMB) and the Office of Personnel Management (OPM), and the Comptroller General of the United States. JFMIP is a joint and cooperative undertaking of OMB, the Department of the Treasury, OPM, and GAO working with executive agencies to improve financial management practices throughout the government.

systems, (4) the increasing importance of managerial cost information to fulfill the objectives of the *President's Management Agenda*, and (5) agency efforts to implement new financial management systems. To develop this testimony, we analyzed the audit reports issued for the 24 CFO Act agencies for fiscal year 2001 and summarized previously issued GAO reports. We also included information from our ongoing work on cost management in the federal government. We conducted our work in accordance with generally accepted government auditing standards.

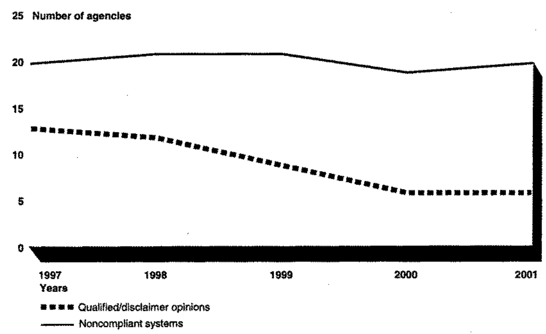
Auditors' Determinations of FFMIA Compliance for Fiscal Year 2001

Most agencies do not yet have timely, accurate, and useful financial information, including cost data, with which to make informed decisions and ensure accountability on an ongoing basis. IGs and their contract auditors reported that the systems of 20 of the 24 CFO Act agencies did not substantially comply with at least one of FFMIA's three requirements for fiscal year 2001. As shown in figure 1, the long-standing weaknesses in agency financial management systems, including internal control issues, can be seen by the steady number of agencies with systems that did not substantially comply with FFMIA over the past several years. In contrast, as also shown in figure 1, the number of qualified or disclaimers of opinions on agency financial statements have steadily decreased over the past 5 years from 13 for fiscal year 1997 to 6 for fiscal years 2000 and 2001. This decrease in qualified and disclaimers of opinions results from monumental efforts in which agencies expend significant resources simply to prepare financial statements. For agencies equipped with modern, fully integrated financial management systems, preparation of financial statements would be more routine and much less costly.

Auditors for four agencies—the Departments of Energy and Labor, the General Services Administration (GSA), and the Social Security Administration provided negative assurance in reporting on FFMIA compliance for fiscal year 2001, meaning that nothing came to their attention indicating these agencies' financial management systems do not meet FFMIA requirements. If readers do not understand the concept of negative assurance, they may have gained an incorrect impression that these systems have been reported by the auditors to be substantially compliant. It is our opinion that because the act requires auditors to "report whether" agency systems are compliant, the auditor needs to provide positive assurance, which would be a definitive statement as to whether agency financial management systems comply with FFMIA. We provide positive assurance on FFMIA compliance for those federal entities for which we conduct financial audits. For example, we reported that the

Internal Revenue Service's financial management systems did not substantially comply with FFMIA. Later in my statement, I will discuss other implications related to FFMIA compliance testing and reporting.

Figure 1: Agency Systems' Compliance with FFMIA 1997 through 2001



Source: Agency audit reports for fiscal years 1997 through 2001.

Widespread Systems Problems Affect FFMIA Compliance

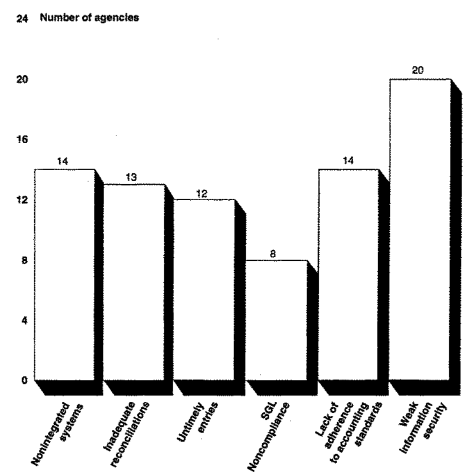
The continuing trend of noncompliance with FFMIA indicates the overall long-standing poor condition of agency financial systems. Correcting the systems problems is a difficult challenge for agencies because of the age and poor condition of their critical financial systems. Some of the federal government's computer systems were originally designed and developed years ago (in some cases, over a decade ago) and do not meet current systems requirements. These legacy systems cannot provide reliable financial information for key governmentwide initiatives, such as integrating budget and performance information.

Based on our review of the fiscal year 2001 audit reports for the 20 agencies reported to have systems not in substantial compliance with one or more of FFMIA's three requirements, we identified six primary reasons. The weaknesses reported by the auditors ranged from serious, pervasive systems problems to less serious problems that may affect one aspect of an agency's accounting operation:

- nonintegrated financial management systems,
- inadequate reconciliation procedures,
- lack of accurate and timely recording of financial information,
- noncompliance with the SGL,
- lack of adherence to federal accounting standards and/or OMB requirements, and
- weak security controls over information systems.

Figure 2 shows the relative frequency that these problems were cited by the auditors at the 20 agencies. However, the auditors may not have reported these problems as specific reasons for lack of substantial compliance with FFMIA. We caution that the degree of noncompliance in a particular category may be even greater since auditors may not have included all problems affecting FFMIA compliance in their reports. For some agencies, the problems are so serious and well known that the auditor can readily determine that the systems lack substantial compliance without examining every facet of FFMIA compliance. Therefore, the reported problems may not be all-inclusive.

Figure 2: Problems Reported by the Auditors for Fiscal Year 2001



Source: GAO analysis of agency audit reports for fiscal year 2001. We did not independently verify or test the data in the agency audit reports.

Nonintegrated Financial Management Systems

According to the CFO Act, each of the 24 agencies is to develop and maintain an integrated accounting and financial management system[3] that

[3]Federal financial system requirements define an integrated financial system as one that coordinates a number of previously unconnected functions to improve overall efficiency and control. Characteristics of such a system include (1) standard data classifications for recording financial events, (2) common processes for processing similar transactions, (3) consistent control over data entry, transaction processing, and reporting, and (4) a system design that eliminates unnecessary duplication of transaction entry.

complies with federal systems requirements and provides for (1) complete, reliable, consistent, and timely information that is responsive to the financial information needs of the agency and facilitates the systematic measurement of performance, (2) the development and reporting of cost information, and (3) the integration of accounting, budgeting, and program information. In this regard, OMB Circular A-127, *Financial Management Systems*, requires agencies to establish and maintain an integrated financial management system that conforms with JFMIP's functional requirements.

An integrated financial system coordinates a number of functions to improve overall efficiency and control. For example, integrated financial management systems are designed to avoid unnecessary duplication of transaction entry and greatly lessen reconciliation issues because transactions are entered only once. Moreover, with an integrated financial management system, an agency is more likely to have reliable, useful, and timely financial information for day-to-day decision making as well as external reporting.

Agencies that do not have integrated financial management systems typically must expend major effort and resources, including in some cases hiring external consultants, to develop information that their systems should be able to provide on a daily or recurring basis. In addition, opportunities for errors are significantly increased when agencies' systems are not integrated. Agencies with nonintegrated financial systems are more likely to be required to devote more resources to collecting information than those with integrated systems. OMB's accelerated reporting dates for agency performance and accountability reports[4] make these major efforts and devotion of resources unsustainable in the long term. In fiscal year 2001, agency performance and accountability reports were due February 27, 2002. In contrast, under OMB's current reporting requirements, agency performance and accountability reports for fiscal year 2002 are due to OMB by February 1, 2003. OMB is further accelerating the deadline so that by fiscal year 2004, agencies will submit these reports by November 15, 2004. With these new accelerated reporting dates, it will be difficult for agencies to continue to rely on significant, costly, and time-intensive manual efforts to achieve or maintain unqualified opinions until automated, integrated processes and systems are implemented that readily

[4]Agency performance and accountability reports include the audit report and the audited financial statements.

produce the necessary information. As a result, many agencies must accelerate their efforts to improve underlying financial management systems and controls, which is consistent with reaching the financial management success measures envisioned by the *President's Management Agenda* and the JFMIP principals.

Auditors frequently mentioned the lack of modern, integrated financial management systems in their fiscal year 2001 audit reports. As shown in figure 2, auditors for 14 of the 20 agencies with noncompliant systems reported this as a problem. For example, the Department of Education's lack of a fully integrated financial management system seriously affects its ability to accumulate, analyze, and present reliable financial information. According to its auditors, Education compiles its financial statements through a multistep process that includes both manual and automated procedures, which increase the risk of errors in the departmentwide financial statements. These manual processes can lead to errors that may affect current and prior fiscal years. For example, Education recorded numerous restatements and reclassifications of prior fiscal year financial statement balances based on its extensive analysis of certain general ledger balances in an effort to resolve errors that existed in past years. While the auditors noted that some of the entries to correct or reclassify amounts resulted from Education's extensive analysis, the identification of these errors reinforces concerns about Education's lack of an integrated financial management system. According to the auditors, Education processed and approved adjustments to correct or reclassify amounts that were later discovered to be erroneous. These new errors resulted in the need for additional manual adjustments to correct these new errors, which cast doubt on the sufficiency of the process for reviewing and approving adjustments. To focus attention on long-standing financial management issues, the Secretary of Education created a Management Improvement Team (MIT). The MIT's goals include addressing outstanding recommendations related to the financial statement audits and ensuring an environment with effective internal controls. The Education IG noted that the MIT has identified corrective actions for improving the department's programs and operations.

The Department of Defense's (DOD) lack of integration between its financial management systems and its other business systems is a critical issue to be addressed in its transformation of business practices. DOD has reported that an estimated 80 percent of the data needed for sound financial management comes from other business operations, such as its acquisition and logistics communities. As we testified in March,[5] DOD's vast array of costly, nonintegrated, duplicative, and inefficient financial management systems reflects the lack of an enterprisewide, integrated approach to addressing its management challenges. DOD's Under Secretary of Defense (Comptroller) has stated that the development of a financial management enterprise architecture[6] is a major step toward achieving the Secretary's goal of transforming DOD's outdated support structure, including decades old financial systems that are not well interconnected. Most recently, DOD selected International Business Machines (IBM) to develop its departmentwide financial management enterprise architecture and set aside nearly $100 million for this effort. According to DOD officials, this reform effort will integrate the department's systems and business processes in the fields of logistics, health care, accounting, finance, personnel and other areas and reduce the more than 1100 stand-alone systems currently generating financial information.

[5]U.S. General Accounting Office, *DOD Financial Management: Integrated Approach, Accountability, Transparency, and Incentives Are Keys to Effective Reform*, GAO-02-497T (Washington, D.C.: March 6, 2002).

[6]An enterprise architecture establishes an agency's roadmap to achieve its mission through the optimal performance of its core business practices within an efficient Information Technology environment. Enterprise architectures are "blueprints" used for defining an agency's current (baseline) and desired (target) environments along with a capital investment roadmap for transitioning from the current to the target environment.

Inadequate Reconciliation Procedures

A reconciliation process, even if performed manually, is a valuable part of a sound financial management system. In fact, the less integrated the financial management system, the greater the need for adequate reconciliations because data for the same transaction may be separately entered in multiple systems, causing the risk of errors to be greater. For example, according to its auditors, the Agency for International Development (AID) places a greater reliance on processes like reconcilations because it lacks an integrated system. Reconciliation of records from the multiple systems would ensure transaction data were entered correctly in each one. Reconciliation procedures are a control necessary to maintain and substantiate the accuracy of the data reported in an agency's financial statements and reports. The Comptroller General's *Standards for Internal Control in the Federal Government*[7] highlights reconciliation as a key control activity.

As shown in figure 2, auditors for 13 of the 20 agencies with noncompliant systems reported that the agencies had reconciliation problems, including difficulty reconciling their Fund Balance with Treasury accounts[8] with the Department of the Treasury's records. Treasury policy requires agencies to reconcile their accounting records with Treasury records monthly, which is comparable to individuals reconciling their checkbooks to their monthly bank statements. However, such reconciliations are not being routinely performed. For example, some of the fund balances with Treasury for the Department of State did not reconcile with Treasury's fund balance amounts. State's auditors reported that the absolute difference[9] between State's and Treasury's balances as of September 30, 2001, was about $131 million. State's auditors noted that while progress had been made in reducing the net difference between State's and Treasury's records, weaknesses in the reconciliation process still remain, particularly affecting older fund balances. The auditors recommended that State reexamine its reconciliation processes and also assess whether adjustments should be made to its records.

[7]U.S. General Accounting Office, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999).

[8]Agencies record their budget spending authorizations in their Fund Balance with Treasury accounts. Agencies increase or decrease these accounts as they collect or disburse funds.

[9]Absolute differences are computed with all numbers considered to be positive numbers.

Inadequate reconciliation procedures also complicate the identification and elimination of intragovernmental transactions. As we testified in April,[10] agencies have not reconciled intragovernmental balances with their trading partners[11] and, as a result, information reported to Treasury is not reliable. For several years, OMB and Treasury have required the CFO Act agencies to reconcile selected intragovernmental activity and balances with their trading partners. However, numerous agencies did not fully perform these reconciliations for fiscal year 2000. Beginning with fiscal year 2001, OMB and Treasury required agency CFOs to report on the extent and results of intragovernmental activity reconciliation efforts. The IGs reviewed these reports and communicated the results to OMB, Treasury, and GAO. IGs reported that the required reconciliations for fiscal year 2001 were not fully performed, citing reasons such as (1) trading partners' not providing needed data, (2) limitations and incompatibility of agency and trading partner systems, and (3) human resource issues. For fiscal years 2001 and 2000, amounts reported for agency trading partners for certain intragovernmental accounts were significantly out of balance. The continued involvement of the CFO Act agencies, the JFMIP principals and OMB will be critical to resolving this issue.

Lack of Accurate and Timely Recording of Financial Information

Accurate and timely recording of financial information is key to successful financial management. Recording transactions timely can facilitate accurate reporting in agencies' financial reports and other management reports that are used to guide managerial decision making. The Comptroller General's *Standards for Internal Control in the Federal Government* states that transactions should be promptly recorded to maintain their relevance and value to management in controlling operations and making decisions. As shown in figure 2, auditors for 12 of the 20 agencies with noncompliant systems found that agencies did not accurately and timely record transactions in the general ledger.

[10]U.S. General Accounting Office, *U.S. Government Financial Statements: FY 2001 Results Highlight the Continuing Need to Accelerate Federal Financial Management Reform*, GAO-02-599T (Washington, D.C.: April 9, 2002).

[11]Trading partners are U.S. government agencies, departments, or other components that do business with each other.

The lack of timely transaction recording can also result in the use of inaccurate information for decision making. For example, auditors for six agencies reported that unliquidated obligations[12] were not deobligated timely due to the lack of procedures for reviewing unliquidated obligations or the failure to follow these procedures. Agency failure to deobligate funds timely may result in the loss of the use of those funds. For example, auditors for the Department of Transportation (DOT) identified about $293 million of obligations that were no longer needed and could be used for other valid purposes or returned to the U.S. Treasury.

Untimely transaction recording during the fiscal year can also result in substantial efforts at fiscal year-end to perform extensive manual financial statement preparation efforts that are susceptible to error and increase the risk of misstatements. For example, auditors reported that Department of Justice components did not perform their accrual-based financial transaction processing on an ongoing basis. Auditors for two components, the Drug Enforcement Administration and the Offices, Boards, and Divisions, stated that the financial statement preparation effort must be a componentwide effort, involving all program budget and administrative offices. Gathering financial data only at year-end does not provide adequate time to analyze transactions or account balances. Without time to perform these analyses, misstated or unsupported financial statement account balances can occur. Further, it impedes management's ability to have timely and useful information for decision making.

[12]The value of goods and services ordered and obligated which have not been paid.

Noncompliance with the SGL

Implementing the SGL at the transaction level is one of the specific requirements of FFMIA. However, as shown in figure 2, auditors for 8 of the 20 noncompliant agencies reported that the agencies' systems did not comply with SGL requirements. The SGL, mandated for use by OMB and Treasury in 1986, promotes consistency in financial transaction processing and reporting by providing a uniform chart of accounts and pro forma transactions. These defined accounts and pro forma transactions are used to standardize the accumulation of agency financial information, as well as enhance financial control and support financial statement preparation and other external reporting. By not implementing the SGL, agencies are challenged to provide consistent financial information across their component agencies and functions. For example, auditors for AID reported that AID does not report on its mission activities[13] using the SGL at the transaction level. These mission activities account for approximately 52 percent of AID's total net cost of operations. AID records its mission activities in its Mission Accounting and Control System—an automated system that uses transaction codes that do not match to the SGL chart of accounts. AID uses a monthly process to crosswalk these mission transactions to the SGL, but cannot ensure that transactions are posted properly and consistently from mission to mission. OMB officials have stated that while this monthly process may be a good interim solution until AID has fully implemented its new core financial system, this process does not allow AID's systems to be substantially compliant with the SGL at the transaction level. Until AID deploys its newly implemented core financial system worldwide, it will continue to use the Mission Accounting and Control System for its overseas missions.[14]

The Department of Housing and Urban Development's (HUD) Federal Housing Administration (FHA) must use several manual processing steps to convert its commercial accounts to SGL accounts. FHA's legacy core financial system, which includes its general ledger, is based on commercial rather than governmental accounting. FHA has 22 systems that feed transactions to its core financial system, 15 of which cannot process transactions in the SGL format. FHA's manual processes include the use of personal computer-based software to convert its commercial accounts to

[13] An AID mission is a representative in a cooperating country. AID has overseas missions and offices that manage projects associated with this foreign assistance.

[14] AID has estimated that the worldwide deployment of the core financial system will not begin until fiscal year 2008.

the SGL. FHA then transfers the balances to HUD's Central Accounting and Program System (HUDCAPS). HUD's auditors noted that FHA's current process does not meet federal financial management systems requirements that a core financial system "provide for the automated and year-end closing of SGL accounts and rollover of the SGL account balances." FHA has completed the initial phases of its project to implement a commercial off-the-shelf (COTS) financial software system. FHA intends to complete implementation of the general ledger module of this COTS system by the beginning of fiscal year 2003, including the implementation of the SGL at the transaction level.

Lack of Adherence to Federal Accounting Standards

FFMIA requires that agencies' financial management systems comply with applicable federal accounting standards, which are developed by the Federal Accounting Standards Advisory Board (FASAB). Agency CFOs are required to use these standards in developing financial management systems and in preparing financial statements. Currently, there are 22 statements of federal financial accounting standards (SFFAS) and 3 statements of federal financial accounting concepts. FASAB continues to deliberate on new and emerging issues that could result in the promulgation of additional standards; therefore, agencies' systems must be able to accommodate any new standards issued in the future.

As shown in figure 2, auditors for 14 of the 20 agencies with noncompliant systems reported that these agencies had problems complying with one or more federal accounting standards. Auditors reported that agencies are having problems implementing standards that have been in effect for some time, as well as standards that have been promulgated in the last few years. Auditors for 3 agencies reported weaknesses affecting compliance with SFFAS No. 7, *Revenue and Other Financing Sources*, which became effective in fiscal year 1998. For example, FHA, a major component of HUD, was reported by the HUD IG to be in violation of the Anti-Deficiency Act due to a lack of systems and processes capable of fully monitoring and controlling budgetary resources. Auditors for 5 agencies reported trouble implementing SFFAS No. 10, *Accounting for Internal Use Software*, which became effective at the beginning of fiscal year 2001.

Auditors for 7 agencies reported problems implementing SFFAS No. 4, *Managerial Cost Accounting Concepts and Standards*. The requirement for managerial cost information has been in place since 1990 under the CFO Act and since 1998 as a federal accounting standard. For example, auditors for the Department of Agriculture stated that the department's systems have not been designed to enable them to provide sufficient and relevant data to comply with SFFAS No. 4. Specifically, the auditors' review of the accounting for user fees at two agencies disclosed that both agencies were not including the full costs of their user fee programs when determining fees. As a result, Agriculture is unable to provide reliable and timely cost information.

Later in my statement today, I will discuss further the impact of managerial cost information on implementation of the *President's Management Agenda.* While SFFAS No. 4 uses the term "managerial cost accounting," some agencies have adopted the term "cost management" instead to emphasize that cost and performance data are needed to improve management decision making and goes beyond the cost data required for external reporting.

Weak Security Controls over Information Systems

Information security weaknesses are one of the frequently cited reasons for noncompliance with FFMIA and are a major concern for federal agencies and the general public. These weaknesses are placing enormous amounts of government assets at risk of inadvertent or deliberate misuse, financial information at risk of unauthorized modification or destruction, sensitive information at risk of inappropriate disclosure, and critical operations at risk of disruption. Auditors for 20 of the 24 CFO Act agencies identified weaknesses in security controls over information systems. Auditors for the 4 agencies that provided negative assurance in reporting on compliance with FFMIA, in their fiscal year 2001 audit reports did not consider the computer security problems identified significant enough to be instances of a lack of substantial compliance with FFMIA. Unresolved information security weaknesses could adversely affect the ability of agencies to produce accurate data for decision making and financial reporting because such weaknesses could compromise the reliability and availability of data that are recorded in or transmitted by an agency's financial management system.

Concerned with reports of significant weaknesses in federal computer systems that make them vulnerable to attack, the Congress enacted Government Information Security Reform (GISR) provisions[15] to reduce these risks and provide more effective oversight of federal information security. GISR requires agencies to implement an information security program that is founded on a continuing risk management cycle and largely incorporates existing security policies found in OMB Circular A-130, *Management of Federal Information Resources*, Appendix III. GISR also added an important new requirement by calling for both annual management and independent evaluations of the information security program and practices of an agency. We recently testified[16] that information security weaknesses were most often identified[17] for (1) security program management, (2) access controls, and (3) service continuity controls. Security program management provides the framework for ensuring that risks are understood and that effective controls are selected and properly implemented. Access controls ensure that only authorized individuals can read, alter, or delete data. Service continuity controls ensure that when unexpected events occur, such as the terrorist attacks on September 11, 2001, critical operations will continue without undue interruption and that crucial, sensitive data are protected. All 24 agencies were reported to have weaknesses in security program management and access controls. Nineteen of the 24 agencies were reported to have weaknesses in their service continuity controls.

Information security weaknesses were cited by auditors for the National Science Foundation (NSF) as an instance in which NSF's systems did not substantially comply with FFMIA's federal financial management systems requirements. [18] Auditors reported that NSF had several weaknesses in its agencywide information security that result in vulnerabilities in logical and physical access controls and has certain vulnerabilities in the design, administration, and monitoring of its controls. Specifically, the auditors noted weaknesses in several areas including (1) application security

[15]These provisions are part of the Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001.

[16]*Information Security: Additional Actions Needed to Fully Implement Reform Legislation*, GAO-02-470T (Washington, D.C.: March 6, 2002).

[17]We analyzed the results of IG and GAO audit reports published from July 2000 through September 2001, including the results of the IGs' independent evaluations.

[18]NSF's systems had been reported to be compliant for fiscal years 1997 through 2000.

design, (2) database security, (3) intrusion detection, (4) physical access, and (5) administration of access privileges. These weaknesses increase NSF's vulnerability to unauthorized viewing, modification, and deletion of financial and other sensitive data, accidentally or deliberately, by internal and external parties. While NSF has been responsive to initiating corrective actions to address these vulnerabilities, limited resources and competing management priorities have affected its ability to fully address these weaknesses.

As we recently reported,[19] the overriding reason that Treasury's Financial Management Service (FMS) continues to have problems related to its computer controls is that FMS does not have an effective entitywide computer security program. Consequently, billions of dollars[20] of payments and collections are at significant risk of loss or fraud, sensitive data are at risk of inappropriate disclosure, and critical computer-based operations are vulnerable to serious disruptions. For fiscal year 2001, the Treasury IG continued to report computer controls as a material weakness at FMS.

Work Performed by Auditors to Determine FFMIA Compliance

While the FFMIA requires auditors to report on the compliance of agency systems with the act in the financial statement audit reports, the assessment of compliance can be performed as a separate review. Moreover, this separate review could be conducted during another period of the year or staggered throughout the year when the auditors' workloads are not as burdensome. While financial statement audits offer some assurances regarding FFMIA compliance, the work needed to assess the compliance of systems with FFMIA is more comprehensive than the testing normally performed as part of a financial statement audit. In performing financial statement audits, auditors generally focus on the capability of the financial management systems to process and summarize financial information that flows into the financial statements. In contrast, FFMIA requires auditors to assess whether an agency's financial management systems comply with systems requirements and provide complete, accurate, and timely information for managing day-to-day operations.

[19] U.S. General Accounting Office, *Financial Management Service: Significant Weaknesses in Computer Controls Continue*, GAO-02-317 (Washington, D.C.: January 2002). We assessed general computer controls over key financial systems as of September 30, 2000.

[20] FMS is the government's financial manager, central disburser, collections agency, as well as its accountant and reporter of financial information.

FFMIA was designed to lead to system improvements that provide agency managers with useful information to measure performance and increase accountability on an ongoing basis, rather than just at year-end.

In our most recent report on FFMIA,[21] we recommended that OMB develop additional guidance, in accordance with the *Financial Audit Manual* (FAM),[22] to specify expected procedures for auditors to perform when assessing FFMIA compliance. This additional guidance should clearly outline (1) the minimum scope of work and (2) the procedures for auditors to perform in determining whether management has reliable, timely, and useful financial information for managing day-to-day operations. Working jointly with representatives from the President's Council on Integrity and Efficiency (PCIE), we have drafted a section for the FAM with detailed audit steps for testing agencies' systems' compliance with FFMIA. If appropriately implemented, these detailed work steps should provide a sufficient basis to conclude as to whether agencies' systems comply with FFMIA. We will continue to work with PCIE to finalize this new section of the FAM.

Remediation Plans Improved but Continue to Lack Important Details

FFMIA requires agency management to prepare remediation plans, in consultation with OMB, that describe the corrective actions they plan to take to resolve their instances of noncompliance, as well as the target dates and resources necessary to bring financial systems into substantial compliance with FFMIA requirements. Although the plans have improved over the years, in the past, we have consistently found that many of these plans lack sufficient detail and descriptions of the resources needed for executing the corrective actions. We are reviewing the remediation plans agencies prepared to address the instances of lack of substantial compliance with FFMIA reported for fiscal year 2000 and will report the results of our analysis in our report to be issued by October 2002.

[21]U.S. General Accounting Office, *Financial Management: FFMIA Critical for Federal Accountability*, GAO-02-29 (Washington, D.C.: October 1, 2001).

[22]The *Financial Audit Manual*, jointly issued by GAO and the President's Council on Integrity and Efficiency, provides the methodology for performing financial statement audits of federal entities.

Increasing Emphasis on Improving Financial Management from the Highest Levels of Government

President's Management Agenda and the Executive Branch Management Scorecard

The administration, with its release of the *President's Management Agenda* in August 2001, has set forth improved financial performance as one of its five governmentwide initiatives. OMB's criteria for measuring improved financial performance include not just getting clean opinions on agency financial statements, but also (1) ensuring that financial management systems meet federal requirements, (2) integrating financial and performance management systems to support day-to-day agency operations, and (3) resolving repeated material weaknesses.[23] This is another area that the JFMIP principals have addressed and on which they are in agreement. The administration plans to use the Executive Branch Management Scorecard, based on OMB's criteria, to highlight agencies' progress in achieving the improvements embodied in the *President's Management Agenda*. This is a step in the right direction to improving management and performance, but the value of the scorecards will be the degree to which the scores lead to sustained focus and demonstrable improvements. It is important that there be continual rigor in the scoring process for the approach to be credible and effective. OMB has provided its baseline scores judging agency financial management as of September 30, 2001, and an updated version of the scorecard will be released during the summer.

JFMIP Principals

In August 2001, the JFMIP principals began a series of periodic meetings that have resulted in unprecedented substantive deliberations and agreements focused on key financial management reform issues, such as better defining measures for financial management success. As mentioned previously, the principals agreed to significantly accelerate financial

[23] A material weakness is a condition that precludes the entity's internal control from providing reasonable assurance that misstatements, losses, or noncompliance material in relation to the financial statements would be prevented or detected on a timely basis.

statement reporting so that the government's financial statements are issued more timely and to discourage costly efforts designed to obtain unqualified opinions on financial statements without addressing the underlying systems challenges. In these meetings, the principals have focused on key issues, some of which I have already highlighted, such as:

- defining success measures for financial management performance that go far beyond an unqualified audit opinion on financial statements and include measures such as financial management systems that routinely provide timely, reliable, and useful financial information and no material internal control weaknesses or material noncompliance with laws and regulations and FFMIA requirements;
- restructuring the FASAB's composition to enhance the independence of the board and increasing public involvement in setting standards for federal financial accounting and reporting;
- establishing audit committees for the major federal agencies;
- overseeing DOD's business transformation efforts;
- monitoring actions to modernize and reduce the cost of routine operations of federal payroll systems; and
- addressing the impediments to an audit opinion on the U.S. government's consolidated financial statements, including intragovernmental transactions.

Future meetings will enable the JFMIP principals to reach agreements and monitor progress on strategies critical to the full and successful implementation of federal financial management reform.

Managerial Cost Information Is Critical for Implementing the *President's Management Agenda*

According to the *President's Management Agenda*, the accomplishment of the other four governmentwide initiatives[24] will matter little without the integration of agency budgets with performance. The lack of a consistent information and reporting framework for performance, budgeting, and accounting obscures how well government programs are performing as well as comparisons of performance and cost across programs. Timely, accurate, and useful financial and performance information can form the basis for reconsidering the relevance or "fit" of any federal program or activity in today's world and for the future. However, even the most meaningful links between performance results and resources consumed are only as good as the underlying data. Therefore, agencies must first address long-standing problems within their financial systems.

Linking of agency budgets with performance is enhanced when agencies integrate managerial cost information into their program activities (or lines of business). For example, Treasury's IG stated that one of the management and performance challenges[25] that Treasury faces is the integration of cost accounting with its business activities. Currently, Treasury managers are unable to link resources to results and often report their accomplishments based on anecdotal performance evidence and outdated financial information.

Agency implementation of managerial cost accounting can be a complex and arduous task. For example, the Federal Aviation Administration (FAA) has been developing a cost accounting system, as required by the Federal Aviation Reauthorization Act of 1996,[26] for several years. DOT's IG recently reported[27] that notwithstanding the progress and successes realized so far, FAA still faces significant challenges to complete and operate a credible

[24]The other four governmentwide initiatives are improved financial performance, strategic management of human capital, competitive sourcing, and expanded electronic government.

[25]U.S. Department of the Treasury, Office of the Inspector General, *Management and Performance Challenges Facing the Department of the Treasury* (Washington, D.C.: January 30, 2002).

[26]This act required FAA to develop a cost accounting system that adequately and accurately reflects the investments, operating and overhead costs, revenues, and other financial measurement and reporting aspects of its operations.

[27]U.S. Department of Transportation, Office of Inspector General, *2001 Status Assessment of Cost Accounting System and Practices, Federal Aviation Administration* (Washington, D.C.: January 10, 2002).

cost accounting system. FAA still needs to (1) implement, on a timely basis, fully developed cost accounting and labor distribution systems, (2) establish cost and performance management practices, (3) account for overhead costs, (4) track assets, and (5) develop an adequate system of internal controls.

Other agencies have adopted various methods of accumulating and assigning costs to obtain managerial cost information needed to enhance programs, improve processes, establish fees, develop budgets, prepare financial reports, and report on performance. A number of agencies have implemented activity-based costing (ABC), which creates a cost model of an organization by identifying the activities performed, the resources consumed, and the outputs (products and services) produced by that organization. ABC then uses accounting and workload data to assign costs to the activities and related outputs. For example, the Small Business Administration (SBA) uses ABC to support financial reporting, management decision making, performance reporting, budgeting, and cost reimbursements. For example, SBA has used information from its cost management system to prepare the Statement of Net Costs, make resource allocation decisions, and provide information for outsourcing alternatives. SBA has also used managerial costing to provide a crosswalk between the costs of activities and programs and the agency's strategic goals and objectives. SBA's cost allocation model provides information about the full costs (direct and indirect) of its programs as well as unit costs for many program outputs. In fiscal year 2001, SBA began using activity-based budgeting (ABB) to analyze program office budgets. The purpose of ABB is to show the linkage between the resources the agency plans to consume and the outputs it plans to produce. ABC and ABB can provide SBA's management with the information needed for sound decision making.

While some agencies have found this method to be useful, ABC is not a universal solution for all organizations. Other agencies have developed managerial costing approaches that build upon existing accounting systems. For example, the Department of the Interior's Bureau of Land Management (BLM) has implemented an innovative cost model that aligns the costs of the bureau's activities with its work processes and mission goals. This model was developed with extensive coordination with field personnel and has been used for management decision making and to develop budget requests. For instance, BLM analyzed information on the costs of various activities associated with its Wild Horse and Burro Program. Based on this analysis, bureau officials formulated a proposal for managing horse and burro populations to achieve appropriate management levels by 2005. They presented their analysis to the House and Senate Appropriations Subcommittees and were provided an additional $9 million for the implementation of the proposal.

Agency Efforts to Implement New Financial Systems

Across government, agencies have many efforts under way to implement or upgrade financial systems to alleviate some of the long-standing weaknesses in financial management. Some of these agencies, including the Departments of Agriculture, Commerce, and Transportation; GSA; and the National Aeronautics and Space Administration (NASA), are in the implementation phases of these projects. Other agencies are in the planning and design phases, such as the Departments of Defense, Energy, and Justice. Many of these new financial systems are COTS packages sold by vendors whose software has been certified by JFMIP.[28]

GSA's IG recently reported[29] that GSA faces significant challenges in implementing its new integrated financial management system solution, Pegasys. GSA had planned to replace its aging and costly-to-maintain current system, the National Electronic Accounting and Reporting (NEAR) system with Pegasys, a COTS product. However, since the project to replace NEAR with Pegasys began, significant modifications have been made to the COTS product to meet specific GSA requirements. The IG reported that the magnitude and complexity involved in modifying a COTS product to meet GSA's needs have been underestimated, necessitating a reassessment of the ability of the COTS product to perform necessary key functions. While the Office of the Chief Financial Officer has rescoped the Pegasys project, numerous technical challenges remain, including completing an enterprise financial management system architecture and adding some critical financial functionality needed before GSA can fully transition to Pegasys.

[28]JFMIP tests vendor COTS packages and certifies that they meet current financial management system requirements for core financial systems.

[29]General Services Administration, Office of Inspector General, *GSA Faces Significant Challenges in Deploying a Fully Integrated Pegasys Financial Management System Solution*, Report Number A010023/B/T/F02205 (Washington, D.C.: January 17, 2002).

NASA is working toward implementing an integrated financial management system that it expects to be fully operational in 2006 at an estimated cost of $475 million. As we testified in March,[30] this is NASA's third attempt to implement a new financial management system. The first two efforts were abandoned after 12 years and spending $180 million. Given the high stakes involved, it is critical that NASA's leadership provide the necessary direction, oversight, and sustained attention to ensure that this project is successful.

As mentioned earlier, DOD has taken a significant step in transforming its business processes by awarding a contract to IBM to develop a departmentwide financial management enterprise architecture. DOD officials have stated that the enterprise architecture will propose new ways of conducting DOD financial activities and offer solutions for modernizing the department's financial practices. DOD faces financial management problems that are pervasive, complex, long-standing, and deeply rooted in virtually all business operations throughout the department. At DOD, overhauling financial management represents a major management challenge that goes far beyond simply installing new software to the very fiber of the department's business operations and management culture. Cultural resistance to change and military service parochialism have played a significant role in impeding previous attempts to implement broad-based management reforms at DOD. The Secretary of Defense has made the fundamental transformation of business practices throughout the department a top priority and has estimated that his envisioned transformation will take 8 or more years to complete. In addition to utilizing sound information technology management practices, DOD needs to address the underlying causes of its inability to resolve long-standing financial management problems, such as providing for sustained leadership; controlling resources; establishing clear lines of authority, responsibility, and accountability; incorporating results-oriented performance measures; providing incentives for action; and ensuring effective oversight and monitoring.

[30]U.S. General Accounting Office, *National Aeronautics and Space Administration: Leadership and Systems Needed to Effect Financial Management Improvements*, GAO-02-551T (Washington, D.C.: March 20, 2002).

Agencies can help ensure that financial management systems investments deliver the intended results by (1) using Clinger-Cohen Act information technology (IT) management requirements, (2) undertaking financial management systems modernization in a broad enterprise architecture context, and (3) redesigning business processes in conjunction with implementing new technology. To assist federal agencies in this process, we have developed the IT Investment Management Framework[31] to provide a common structure for discussing and assessing IT capital planning and investment management practices. This framework has five maturity stages, which represent steps toward achieving both a stable and mature IT investment management process. Other key factors for successful implementation include having top management commitment, adequate funding, and staff with the right skill mix.

Once a project has been selected, good project management is a critical ingredient to successful implementation. For example, it is imperative that managers sufficiently plan their project and that the sponsors are involved in the implementation. Next, deadlines should be realistic and project managers should be capable of understanding the complexities of the job. Throughout the job, the implementation should be monitored to ensure the project is going as planned.

Closing Comments

The primary purpose of FFMIA is to ensure that agency financial management systems routinely provide reliable, useful, and timely financial information so that government leaders will be better positioned to invest resources, reduce costs, oversee programs, and hold agency managers accountable for the way they run programs. While many agencies are receiving unqualified opinions on their financial statements, auditor determinations of FFMIA compliance are lagging behind. To achieve the financial management improvements envisioned by the CFO Act, FFMIA, and more recently, the *President's Management Agenda*, agencies need to modernize their financial systems to generate reliable, useful, and timely financial information throughout the year and at year-end. Today, we are seeing a strong commitment from the President, the JFMIP principals, and the Secretaries of major departments, such as DOD, to ensuring that these needed modernizations come to fruition. This commitment is critical to the

[31] U.S. General Accounting Office, *Information Technology Investment Management: An Overview of GAO's Assessment Framework* (Exposure Draft), GAO/AIMD-00-155 (Washington, D.C.: May 2000).

success of the efforts under way and those still in a formative stage and must be sustained. Finally, Mr. Chairman, the leadership demonstrated by you and the members of this subcommittee has been an important catalyst to reforming financial management in the federal government. Continued attention to these issues will be critical to sustaining momentum on financial management reform efforts.

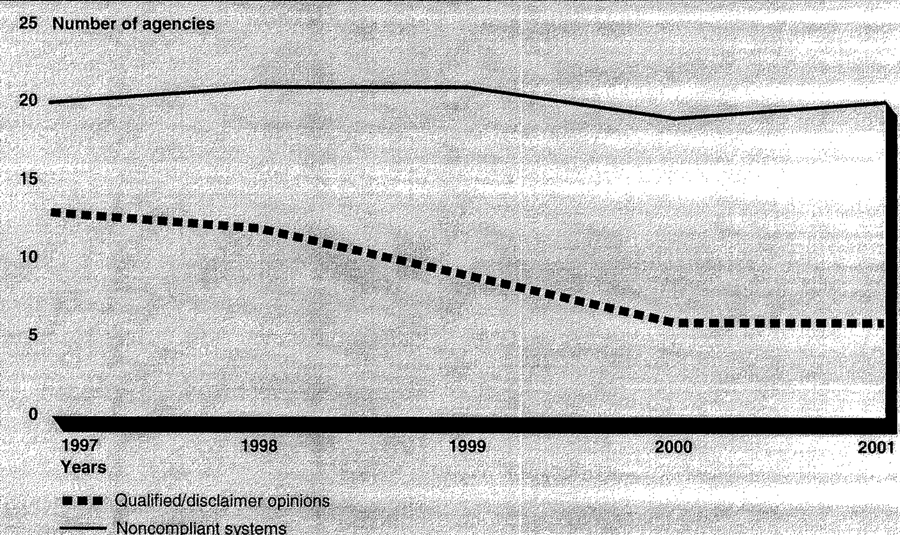
Mr. Chairman, this concludes my statement. I would be pleased to answer any questions you or other members of the subcommittee may have at this time.

Contacts and Acknowledgments

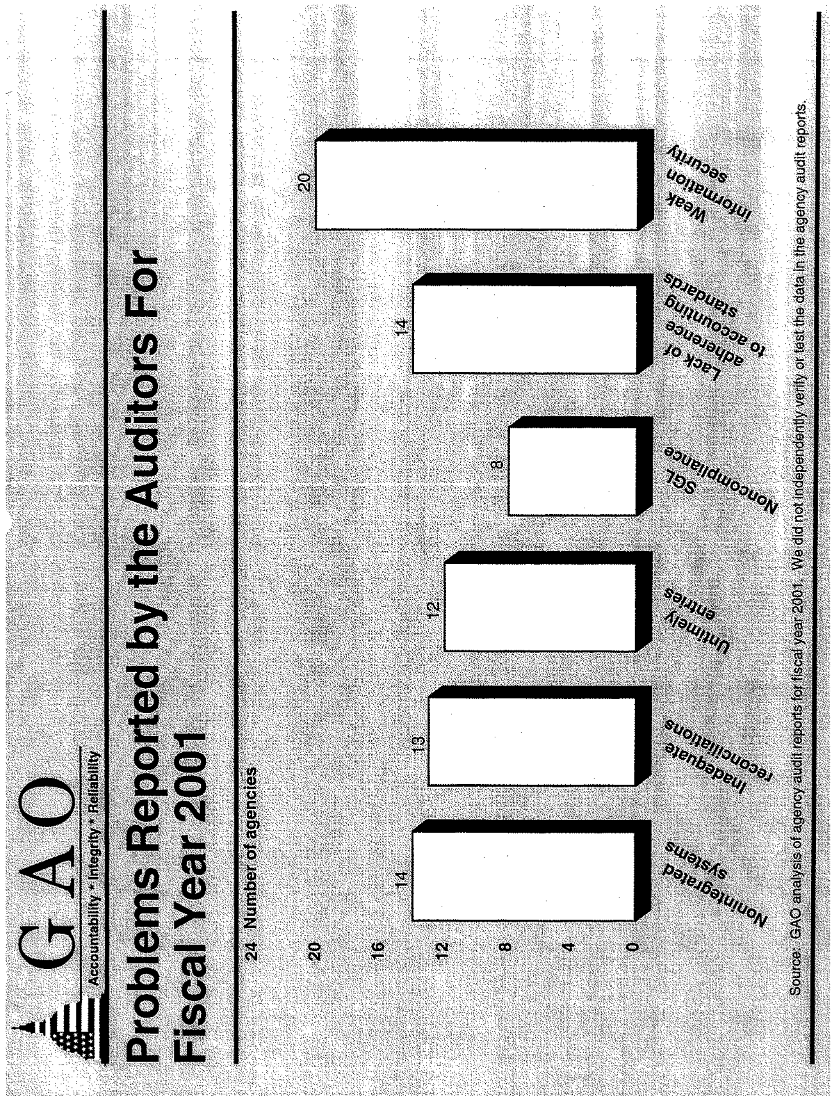
For further information about this statement, please contact Kay L. Daly at (202) 512-9312. Other key contributors to this testimony include William S. Lowrey, Debra S. Rucker, Sandra S. Silzer, and Bridget A. Skjoldal.

GAO
Accountability * Integrity * Reliability

Agency Systems' Compliance with FFMIA 1997-2001



Source: Agency audit reports for fiscal years 1997-2001


GAO
Accountability * Integrity * Reliability
Problems Reported by the Auditors For Fiscal Year 2001
24 Number of agencies
20
16
12
8
4
0
14
Nonintegrated systems
13
Inadequate reconciliations
12
Untimely entries
8
SGL Noncompliance
14
Lack of adherence to accounting standards
20
Weak information security
Source: GAO analysis of agency audit reports for fiscal year 2001. We did not independently verify or test the data in the agency audit reports.

Mr. HORN. Well, thank you very much.

We have on the floor a motion, and we have to go over and answer to it. So we're going into recess now. Relax.

[Recess.]

Mr. HORN. We were in recess and out of it. And I'm sure we've saved the Nation much from taking that amendment that would close us down. So we're going to close them up.

But anyhow—so, we'll go on with Karen Alderman, Executive Director, Joint Financial Management Improvement Program. We look forward to your testimony.

STATEMENT OF KAREN CLEARY ALDERMAN, EXECUTIVE DIRECTOR, JOINT FINANCIAL MANAGEMENT IMPROVEMENT PROGRAM

Ms. ALDERMAN. Thank you, Mr. Chairman. I'd like to submit my statement for the record and provide brief remarks.

Mr. HORN. Your statements are automatically put in the record when I call your name.

Ms. ALDERMAN. OK.

The President's management goal to improve financial management requires quality systems, data and processes. Currently, most Federal agencies use custom development—custom-developed financial systems that are antiquated and unable to support current requirements of FFMIA.

Also, the Federal Government is moving to commercial off-the-shelf software to meet their needs. In 1998, 40 percent of financial applications under development that are being phased in were commercial off-the-shelf software. In 2001, 60 percent were.

JFMIP has focused its recent activities on functional requirements for financial systems, software qualification testing, the intergovernmental transactions and elimination study, financial management and human capital and information sharing and outreach.

Regarding financial system requirements, JFMIP's role is to identify and clearly describe those requirements in a series of documents so that they're readily available to agencies, auditors, vendors and other stakeholders. The JFMIP Framework for Federal Financial Management Systems, issued in 1995, identified 15 components of the Federal financial management system including core managerial cost accounting and 13 subsidiary systems. At the time the FFMIA was passed in 1996, the Core Financial System and six of the subsidiary requirement documents had been issued one time and many of those were out of date.

Starting in 1998, JFMIP began an intensive effort to update these documents, 10 have been issued between 1998 and 2001, and we're currently working in partnership with the Procurement Executive Council to issue acquisition and financial system interface requirements. We have also worked to develop non-income tax revenue system requirements, and we have recently partnered with the CIO Council to update the framework document for the incorporation of the Clinger-Cohen Act and produce the financial segment of the Federal Enterprise Architecture.

In addition to the requirements, we have worked to test and qualify Core Financial Systems. This process was initiated in 1999.

The components are up-to-date Core Financial System Requirements, an open and comprehensive testing and qualification process, establishment of an open knowledge base for all to see what those test requirements and outcomes are, and a change in OMB policy that mandated that Federal agencies use qualified software when acquiring new COTS systems for Core Financial Systems. This process transition occurred October 1, 1999. Ten software products offered by eight vendors and one government software cross-service provider were qualified under the 1999 test and the 2000 incremental test. In 2002, about half the existing certificates will expire, and the balance will expire in 2003.

JFMIP designed the test process to ensure that Federal requirements and vendor offerings remained aligned. We have a feedback mechanism to update requirements, and in 2002 we will update that test based on the requirements issued in November 2001. We updated those requirements based on feedback from the agencies about what was working, and what did not work as well and needed clarification. Areas like upward and downward adjustments and better closing processes were identified, and also new requirements were added to capture more information on full cost and revenue to unique cost objectives, as well as daily internal reports.

In general, revisions will help ensure that core software has functionality to support the financial aspects of performance reporting required under the President's Management Agenda.

Our second round of testing, which will be finalized at the end of this summer, will basically double the amount of test steps to more thoroughly test existing requirements and new requirements.

In addition to these two agendas, I'd like to briefly mention intergovernmental elimination and financial management human capital. The intergovernmental elimination study undertaken in 2001 was to address problems identified that make it difficult for the government to properly identify intergovernmental transactions and balances and allow the U.S. Government a consolidated financial statement to achieve a clean opinion.

The study found that the quality of the financial data throughout the Federal Government is poor. Agencies cannot identify their true business partners and, consequently, reconcile the differences that may exist. Common standards and business practices to support consistent recording of events are missing and technology needs to be applied. OMB is undertaking efforts today to address these issues.

Thank you very much.

Mr. HORN. Thank you.

[The prepared statement of Ms. Alderman follows:]

Statement by Karen Cleary Alderman, Executive Director
Joint Financial Management Improvement Program (JFMIP)
Before the
Subcommittee on Government Management, Information, and Technology
Committee on Government Reform
June 6, 2002

Thank you for the opportunity to discuss the role of the Joint Financial Management Improvement Program (JFMIP) in supporting the goals of the Federal Financial Management Improvement Act (FFMIA). The mission of the JFMIP is to improve financial management practices in the Government through the joint and cooperative efforts of the U.S. Department of the Treasury (Treasury), the General Accounting Office (GAO), the Office of Management and Budget (OMB), the Office of Personnel Management (OPM), and all Federal agencies. Major JFMIP responsibilities with respect to Federal financial management systems include issuing Federal financial system requirements, testing and qualifying core financial system software for Federal agency use, and facilitating information exchange among all stakeholders, both in the public and private sectors. My testimony highlights ongoing JFMIP efforts in these areas.

Financial management systems that support Federal accounting needs are one of the key pillars for achieving the improvement in financial management envisioned by the CFO Act. The vision for Federal financial management systems is to support a partnership between program and financial managers to assure the integrity and availability of information for decision-making and performance measurement. To achieve that vision, Federal financial systems need to:

- Produce accurate, timely, complete, reliable and consistent information
- Provide adequate agency management reporting
- Support governmentwide and agency policy decisions
- Support preparation and execution of agency budgets
- Facilitate financial statement preparation
- Provide information to central agencies
- Provide cost information for agency decision-makers, and
- Provide audit trail information

Without timely, accurate, and consistent financial data, it is difficult, at best, to make informed decisions regarding the delivery of Federal programs. The importance of financial systems in providing this functionality is indisputable. The passage of the FFMIA in 1996 reemphasized the need for Federal financial systems to support the building blocks of financial and performance information by placing in statute three existing policy requirements. Section 803 (a) requires that each agency shall implement and maintain financial management systems that comply substantially with Federal financial management systems requirements, applicable Federal accounting standards, and the U.S. Government Standard General Ledger at the transaction level.

Many Federal financial systems are antiquated, stovepiped and unable to provide critical financial information on a timely basis or to support new requirements. Currently, most financial management systems used by Federal agencies are internally developed products. However, the Federal government is moving to commercial off-the shelf-software (COTS). In 1998, 40 percent of applications under development or being phased in were commercial- off-the-shelf software. In 2001, 60 percent of applications under development or being phased in relied on COTS.

Financial systems improvement has been a priority within the financial management community for several years. The President's management goal to improve financial performance requires quality financial systems, data, and processes. In concert with our stakeholders and the CFO Council's Systems/E-government Committee, JFMIP focused its recent activities in these major areas:

- functional requirements for financial systems
- software qualification testing
- intragovernmental transactions and eliminations study
- financial management human capital
- information sharing and outreach.

JFMIP activities are funded by contributions from the JFMIP Principals, in the amount of $570,000, under section 628, of the Treasury and General Government Appropriations Act, 2002, and by contributions from Federal agencies, in the amount of $2,400,000 under section 629 of the same Act. This $3 million annual investment enables the retention of a mix of highly qualified staff as well as access to private sector experience through consultants to provide longer-term strategic solutions to long-standing shortfalls in Federal financial systems. JFMIP has a long history of support and cooperation from all Federal agencies.

Financial System Requirements

Defining governmentwide systems functional requirements necessary to support statutes, Executive Branch policies and regulations, and Federal accounting standards is critical for achieving the desired improvement in financial systems and financial information. JFMIP's role is to analyze, collate, summarize, and publish these requirements in the JFMIP series of system requirement documents so that the requirements are readily available to agencies, auditors, vendors, or anyone who needs them.

The JFMIP *Framework for Federal Financial Systems*, issued in 1995, identified 15 components of a financial management system. The components of an integrated financial management system include the core financial system (inclusive of a financial reporting system), managerial cost accounting system, and 13 subsidiary financial systems. Upon passage of the FFMIA in 1996, requirement documents existed for the Core Financial System and 6 subsidiary systems. Several of those documents needed to be updated to recognize recently enacted laws and regulatory revisions.

Since 1998, JFMIP has been engaged in an intensive effort to update system functional requirements documents. In 1998, *Managerial Cost Accounting System Requirements* was issued. In 1999, JFMIP published updated system requirements for core financial systems, human resources and payroll, travel, and direct loans. In 2000, JFMIP updated system requirements for seized property and forfeited assets, and guaranteed loans. In addition, grant financial system requirements and property management system requirements were published for the first time ever. In 2001, JFMIP issued benefit system requirements and worked collaboratively with the Procurement Executive Council to gather and summarize requirements that interface acquisition and financial systems. The *Acquisition/Financial Systems Interface Requirements* document is now being finalized. JFMIP initiated work on non-income tax revenue system requirements. Finally, JFMIP recently partnered with the CIO Council to update the *Financial Management Systems Framework* document to incorporate the requirements of the Clinger-Cohen Act and to produce the financial segment of the Federal Enterprise Architecture. The current status of the JFMIP financial system requirements documents is shown at Figure 1. This work facilitates improved Federal financial management systems in the future.

In November 2001, JFMIP updated *Core Financial System Requirements*, previously issued in February 1999. The update reflects the results of a comprehensive review to determine areas for improvement. Requirements were clarified in areas such as Treasury payment requirements, upward/downward adjustments for prior-year recoveries, and expanded the trading partner code to support intragovernmental transactions and year-end closing process. New requirements were added to capture full cost and revenue to unique cost objects, and daily internal reports requirements were expanded and enhanced. In general, the revisions will ensure that core software has functionality to support financial aspects of performance reporting required by several elements of the President's management agenda. The updated requirements document is the basis of the redevelopment of the JFMIP core software qualification test.

Core Financial System Testing and Qualification Process

The CFO Council and the JFMIP have partnered to greatly enhance the Core Financial Systems testing qualification and procurement processes to improve the availability of commercial software that supports Federal requirements and to improve the chances that agencies can successfully implement new systems. JFMIP tests core financial system software and issues a 3-year certificate of compliance to versions of software packages that pass 100 percent of test steps. Over half of the existing certificates will expire at the end of fiscal year 2002.

Prior to 1999, testing of core financial system software was accomplished in connection with the mandatory General Services Administration schedule for Financial Management System Software (FMSS). Information regarding the testing process was limited. The test addressed less than one third of the existing requirements. Arrangements for the software testing relied upon agency volunteers and other ad hoc approaches. Past experiences indicated that these arrangements were not sufficient to meet the challenge. In 1998, the CFO Council recommended: (1) the establishment of a Program

Management Office (PMO) under the JFMIP with responsibility for developing the tools and capabilities necessary to improve financial systems across the Federal government; (2) the separation of the test and qualification process from the procurement process; and (3) the establishment of an electronic Knowledgebase (www.jfmip.gov) to share information widely.

October 1, 1999, marked the transition from the old process to a new process. Since that time, JFMIP has completed one cycle of testing, and has embarked on the second cycle of testing. The components of this process are:

- Current core financial system requirements with a continuous feedback mechanism with Federal agencies to clarify and strengthen requirements.

- An open and comprehensive testing and qualification process that test, in part or in whole, mandatory requirements. Through JFMIP's feedback mechanism with Federal agencies and vendors, the process results in a continuous "raising of the bar" that core financial software must meet. The current second round of qualification testing represents a significant higher level of requirements, which will result in a major improvement to the core financial software available to Federal agencies.

- OMB Policy --Circular A-127, "Financial Management Systems" –that requires Federal agencies to use JFMIP qualified software when acquiring commercial core financial system software.

- Establishment of a web-based "Knowledgebase", www.jfmip.gov, to share information with all stakeholders on all parts of the process.

The purpose of testing is to reduce the risk to the Government in procuring core accounting software, produce useful information, reduce agency test effort and provide critical information to commercial business partners to allow them to be successful in providing core accounting software that meets Federal requirements. Currently 10 software products offered by 8 vendors and one government cross-service provider are qualified based on the 1999 test and the 2000 incremental test for FACTS II and other functionality.

JFMIP testing is designed to ensure that Federal requirements and vendor offerings remain aligned. About half of the existing certificates will expire at the end of fiscal year 2002, the rest will expire in FY 2003. JFMIP began the redevelopment of our core software qualification test during fiscal year 2001. The staff met with agencies and vendors to solicit comments on the existing test. JFMIP also commissioned a review of the qualification test to determine what improvements could be made.

JFMIP is completing the second qualification test based on the latest core financial system requirements, dated November 2001. JFMIP's second qualification test includes over 1000 test steps that fully or partially test the majority of the mandatory requirements. This test is being validated with help of the GAO and an independent "software integrator". During FY 2002-2003 all software will be required to take the second qualification test to demonstrate compliance with the latest requirements.

The JFMIP "Knowledgebase", at www.jfmip.gov, provides rapid and efficient communication among government and private sector stakeholders. Currently it hosts database information on core financial systems requirements, test materials, reference materials, qualified software and best practices. We also publish a test trace matrix to fully disclose the relationship between established requirements and test steps. This matrix also identifies the limit of test data so that agencies have full information about the depth of the test and any requirements that agencies must test prior to their software procurement. The website also contains the *Financial Systems Road Map,* which is a resource library to directly support agency project managers, staff, and vendors with information to help successfully implement financial systems. We have had about 150,000 hits on this site over the last two years.

Other JFMIP Efforts to Improve Financial Management Systems

In addition to the above initiatives, I would like to highlight two other initiatives where JFMIP is partnering with the CFO Council and other stakeholders to leverage resources and address common financial management system challenges. These include intragovernmental eliminations and financial management human capital.

Intragovernmental Eliminations Study. After several years of effort, it is still not possible to properly eliminate intragovernmental transactions and balances in the U.S. Government's Consolidated Financial Statements. Inability to eliminate these amounts affects the Government's ability to determine its cost of operations which, in turn, impairs the Government's ability to control and reduce costs, assess performance, evaluate programs, and set fees to recover costs where required. Additionally, many agencies are still having difficulty eliminating intragovernmental transactions and balances within their own agencies.

In 2001, JFMIP studied issues associated with the recording, reporting and elimination of intragovernmental transactions and balances. Findings included:

- The quality of the financial data throughout the Federal government is poor;
- Agencies cannot identify their business partners and thus cannot reconcile any differences that may exist;
- Common standards for data, business practices, and consistent recording of events are missing; and
- Technology must be used to address these issues and overcome limitations in installed financial systems and human capital.

Based on JFMIP staff findings, OMB will improve technical tools and procedural guidance for agencies as well as develop functional and data architecture to support the intragovernmental business process. Actions are already underway as part of the

Integrated Acquisition Environment, one of the 24 initiatives under the President's management agenda for e-government.

Financial Management Human Capital. JFMIP has worked with the Human Resources Committee of the CFO Council since 1995 on the development of core competencies for financial management personnel. The knowledge, skills and abilities that are identified as core competencies have been issued for accountants, budget analysts, and financial system analysts. Core competencies in financial management have been developed for program managers, information technology personnel implementing financial systems, and management analysts and financial specialists.

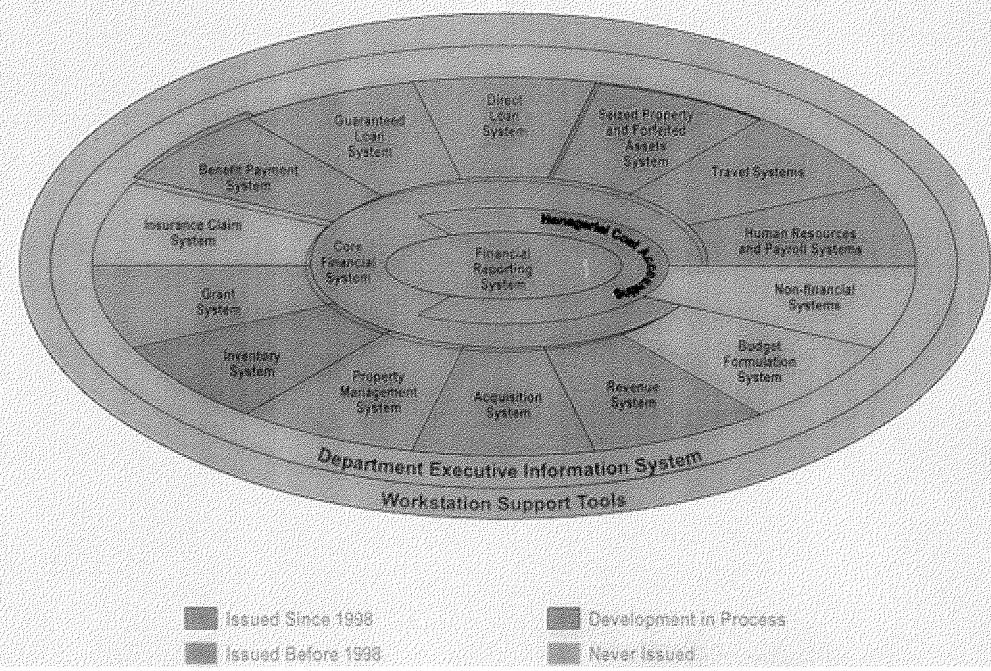
In 2001 JFMIP completed the development of core competencies in financial management for project managers implementing financial systems. In 2002, JFMIP published *Building the Work Force Capacity to Successfully Implement Financial Systems* which recommended ways to improve the recruitment, retention and training of personnel working on financial system implementation. Some agencies are implementing these recommendations to improve their work force to implement commercial off-the-shelf financial systems.

Conclusion

In summary, the leveraging of resources through JFMIP to provide system requirements, testing, and tools demonstrates commitment among Federal stakeholders to address common system challenges in a cost-effective manner. The short-term payoff has been to reduce agencies' cost and risk in replacing systems. The longer-term payoff will be the implementation of Federal financial management systems that fulfill the goals of FFMIA.

Figure 1.

Status of JFMIP Financial Management Systems Requirements Documents, June 2002



Mr. HORN. And we now move to your colleague, Lloyd A. Blanchard, Ph.D., Chief Operating Officer, Small Business Administration.

Glad to have you here, Mr. Blanchard.

STATEMENT OF LLOYD A. BLANCHARD, Ph.D., CHIEF OPERATING OFFICER, SMALL BUSINESS ADMINISTRATION

Mr. BLANCHARD. Thank you, Mr. Chairman, and good morning. Thank you for inviting the Small Business Administration to offer testimony today on the agency's financial management program, and specifically its efforts to comply with Federal Financial Management Improvement Act of 1996.

Let me start by saying that improving financial management is one of the goals of the President's Management Agenda and therefore is a top priority of SBA. With the active involvement of SBA's Administrator, Hector Baretto, the Agency has recently put into place a top-flight management team to accomplish this goal. As one of the 24 principal agents, he's named in the Chief Financial Officers Act of 1990. SBA has a career CFO, Tom Dumaresq, who is here with me today and reports directly to the Administrator to oversee SBA's financial management program.

As Chief of Operations, I work closely with the CFO to ensure coordination and integration of all strategic management decisions and general operations with SBA's financial management program.

The Federal Financial Management Improvement Act requires enhanced compliance in three specific areas: financial management system requirements, Federal accounting standards, and the general ledger and the standard general ledger. These requirements and the other budget and performance initiatives SBA has undertaken are part of the Agency's comprehensive financial management program to provide the taxpayer and Congress full assurance that SBA is acting as good stewards of its appropriated resources.

SBA has an aggressive internal control program, one that mitigates risk by ensuring a positive control environment. The best written procedures in the world would not be effective without the active involvement of senior management conveying the message that integrity cannot be compromised. Moreover, SBA produces annual financial statements that are audited by an independent public accounting firm under contract with SBA's Office of the Inspector General.

I am proud to report that SBA has been recognized as a leader in its development of a cost information management system which is based on an activity-based costing model allowing for full cost allocation on all SBA activities. SBA continues to fine tune this model.

As required by the President's Management Agenda, SBA is integrating this cost information into its planning and decision processes for the fiscal year 2003 and 2004 budget cycles. While President Bush has recognized the need for improvement in this area, Federal financial management guidelines are extremely complex, and SBA faces a difficult task to make the changes necessary for improvement. Thus, in an effort to stay ahead of the curve on new statement reporting requirements, SBA implemented OMB bulletin

01–09 for its fiscal year 2001 reporting 1 year earlier than required.

In the attempt to understand and implement these substantial changes, production of the fiscal year 2001 financial statements was delayed in getting to the auditors and included some mathematical and classification errors. While these errors were corrected in the final statements and the audit was completed on time, the delay in the internal review process produced material weakness on the timeliness and quality of information provided in SBA's reporting process.

Mr. Chairman, although this was very disappointing, SBA believes it made the right decision at the time and will be in a better position for the future because of it. More challenges still lie ahead for us, and to be successful, SBA will need to place more attention on improving its financial management, especially in replacing ineffective and outdated financial systems and processes.

In fiscal year 2000, SBA decided to purchase a financial management system using Oracle software and implement this system beginning in fiscal year 2002. As planned, SBA did bring the new system online at the beginning of the fiscal year. While the later versions—while the later versions have been implemented throughout the government, their earlier Oracle system has not been widely implemented in the Federal Government, and consequently, the true results and cost of the system to SBA are still relatively unknown. To date, the system has had much less functionality and produced much higher cost than we expected. SBA is still in the process of working out these implementation bugs, Mr. Chairman.

Closing fiscal year 2002 under this system can still prove to be a challenge to SBA at the end of the year as the end of the fiscal year rapidly approaches. These difficulties have led SBA to review contingency options, including moving to the latest release much earlier than we had originally expected.

Mr. Chairman, let me conclude my statement by reiterating that SBA is fully committed to continuing the improvements of its financial management processes and systems. While the Federal guidelines and the President's Management Agenda drive SBA toward accomplishing this end, it is simply the right thing to do. It is only with modern systems, transparent reporting, sound and accurate financial information and accountability that the performance of SBA's programs will be able to be accurately evaluated. This will give SBA the opportunity to improve efficiency and effectiveness in services and programs. This is what the President and Congress expect, the taxpayer demands, and SBA intends to deliver.

Thank you, Mr. Chairman. I'm happy to answer any questions that you or other members of the subcommittee may have.

Mr. HORN. Thank you.

[The prepared statement of Mr. Blanchard follows:]

STATEMENT OF

LLOYD A. BLANCHARD

CHIEF OPERATING OFFICER

U.S. SMALL BUSINESS ADMINISTRATION

FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT

BEFORE THE

SUBCOMMITTEE ON GOVERNMENT EFFICIENCY, FINANCIAL MANAGEMENT AND INTERGOVERNMENTAL RELATIONS

COMMITTEE ON GOVERNMMENT REFORM

UNITED STATES HOUSE OF REPRESENTATIVES

JUNE 6, 2002

Good Morning Mr. Chairman, Ranking Member, and Subcommittee Members. My name is Lloyd Blanchard. I am the Chief Operating Officer (COO) at the U.S. Small Business Administration (SBA). Thank you for inviting SBA to offer testimony today on the Agency's financial management program and specifically its efforts to comply with the Federal Financial Management Improvement Act (FFMIA) of 1996.

Let me start by saying that improving financial management systems is a top priority for SBA, and the Agency has put into place a top-flight management team to accomplish this goal. This is the direct result of the active involvement of SBA Administrator Hector Barreto. As one of the 24 principal Agencies named in the Chief Financial Officers (CFO) Act of 1990, SBA has a career CFO, Tom Dumaresq, who reports directly to the Administrator, to oversee SBA's financial management program. I work closely with the CFO to ensure coordination and integration of all strategic management decisions and general operations of the Agency with SBA's financial management program.

The Federal Financial Management Improvement Act requires enhanced Federal compliance in three specific areas: financial management system requirements; Federal accounting standards; and the Standard General Ledger. These requirements and the other budget and performance initiatives SBA has undertaken are part of the Agency's comprehensive financial management program to provide the taxpayer and Congress full assurance that SBA is acting as good stewards of their dollars.

SBA has an aggressive internal control program, one that mitigates risk by ensuring a positive control environment. The positive "tone at the top" conveys the message that integrity cannot be compromised. SBA produces annual financial statements that are audited by an independent public accounting firm under contract with SBA's Office of the Inspector General.

SBA has been recognized as a leader in its development of a cost accounting system. It is an activities-based costing model, allowing for full cost allocation on SBA activities. SBA continues to fine-tune this model. As required by the President's Management Agenda, SBA is integrating this cost information into its planning and decision processes for the FY 2003 and FY 2004 budget cycles.

SBA is considered one of the five largest Federal credit agencies due to its large credit and capital programs and its management of a loan portfolio of approximately $50 billion dollars. This status places SBA in the same class as the Departments of Education, Veterans Affairs, Agriculture, and Housing and Urban Development. SBA is nowhere near the size and complexity of these large Departments yet is required to have the same extensive financial management program, including the same complex financial systems, reports, statements, and fiscal activities. This is a continuing challenge, and SBA strives to be creative and innovative in addressing it. Fortunately, being smaller, fewer layers of bureaucracy have allowed SBA to get decisions more quickly and see results faster.

SBA's CFO office has substantial institutional knowledge in all areas of Federal financial management and, in fact, is a leader in several areas within the Federal financial community.

SBA conducts some of the most sophisticated analysis of loan performance under the Federal Credit Reform Act. SBA has been aggressively using electronic commerce for its transactions for many years and starting in FY 1996 was the first Federal Credit Agency to receive a clean, or unqualified, opinion. SBA has maintained this for six consecutive years.

SBA Financial Statement Results

Fiscal Year	Opinion	Findings	Material Findings	FFMIA Compliant?
1991	Qualified	10	0	No
1992	Qualified	6	3	No
1993	Qualified	6	3	No
1994	Qualified	4	2	No
1995	Qualified	6	3	No
1996	Unqualified	6	1	No
1997	Unqualified	3	2	No
1998	Unqualified	3	3	No
1999	Unqualified	2	2	No
2000	Unqualified	1	0	Yes
2001	Unqualified	4	1	No

However, SBA cannot afford to rest on its laurels. President Bush has identified need for fundamental change in Federal financial management programs and systems across the entire Federal government as part of his management agenda. This has been and remains a high priority for SBA. Federal guidelines in these areas are extremely complex, and SBA faces a difficult task to make the changes necessary for improvement. A large part of this is making financial statements' "form and content" more meaningful and accelerating their production. The Office of Management and Budget's (OMB) issuance of OM bulletin 01-09, "Form and Content of Agency Financial Statements," last year making fundamental and necessary changes to the statements "form and content" underscores the importance of this challenge.

In an effort to stay ahead of the curve on the new statement reporting requirements, SBA implemented OMB bulletin 01-09 for its FY 2001 reporting, one year earlier than required. In the attempt to understand and implement these substantial changes, production of the FY 2001 financial statements was delayed in getting to the auditors and included some mathematical and classification errors. These errors were corrected in the final statements, and the audit was completed on time. However, the delay in SBA's internal schedule and internal review process gave SBA a material weakness on the timeliness and quality of information provided in its financial statement process. SBA's noncompliance with FFMIA with accounting standards and integrated financial management systems caused a slippage in the President's Management Agenda Scorecard Financial Performance rating from a "YELLOW" to a "RED."

Mr. Chairman, as you can imagine, this perceived step backwards scorecard and audit opinion was very disappointing. However SBA believes it made the right decision at the time and will be in a better position for the future because of it. More challenges still lie ahead for us, especially related to the continued acceleration of the reporting deadline – leading to a November 15 date for FY 2004 financial statements in just two years. To be successful, SBA will need to place more attention on improving its financial management, including the replacement of outdated financial systems and processes.

In FY 2000, SBA decided to purchase a financial management system based on Oracle software and implement this system at the beginning of FY 2002. A new system, or a cross-servicing agreement with a different agency, was necessary because a cross-servicing agreement with the Department of Treasury was being discontinued at the end of FY 2002. This new

Oracle system was running on October 1, 2001. To date, the system has much less functionality and much higher costs than expected. SBA is still working out implementation bugs since the software was brought on-line. Closing FY 2002 under this new system still could prove to be a challenge to SBA as the end of the fiscal year rapidly approaches. SBA is currently reviewing its options. The Oracle system has not been widely implemented throughout the Federal government, and the true results and costs of the system for SBA are relatively unknown.

Mr. Chairman, let me conclude my statement by reiterating that SBA is fully committed to continue to improve its financial management processes and systems. The President's Management Agenda drives SBA towards accomplishing this end, and it is the right thing to do. Now is the time for SBA to fully embrace these and move forward. It is only with modern systems, transparent reporting, sound and accurate financial information, and accountability that the performance of SBA's programs will be able to be accurately evaluated. This will give SBA the opportunity to improve efficiency and effectiveness in services and programs. This is what the President and Congress expect, the taxpayer demands, and SBA intends to deliver.

Thank you Mr. Chairman, I am happy to answer any questions that you or other Members of the Subcommittee may have.

Mr. HORN. Our last presenter is Donna R. McLean, Assistant Secretary for Budget and Programs and Chief Financial Officer of the Department of Transportation.

Give my regards to your Secretary. It doesn't matter whether he's a Democrat or a Republican; he's a great public servant.

STATEMENT OF DONNA McLEAN, ASSISTANT SECRETARY FOR BUDGET AND PROGRAMS AND CHIEF FINANCIAL OFFICER, U.S. DEPARTMENT OF TRANSPORTATION

Ms. MCLEAN. Thank you, sir.

Mr. Chairman, I appreciate the opportunity to discuss DOT's progress in achieving its goals for the Federal Financial Management Improvement Act of 1996. And today I will answer your questions regarding why DOT is not yet compliant with FFMIA, what we are doing about it, and the challenges we are still facing in trying to become compliant with the FFMIA.

Within DOT, we take financial management very seriously and put a significant amount of energy and effort into taking care of the public's money. Part of our stewardship role is to clearly show DOT's performance and what benefits have been provided by the funds received.

Our performance report was selected as the "Best in Government" this year by the Mercatus Institute. We want our financial management to reach this same level. The standards for success for financial management, as outlined in the President's Management Agenda, lay a roadmap showing us the way, and clearly achieving full compliance with the requirements of FFMIA is critical to our success.

In our quest for success, DOT has faced a number of challenges in reaching full compliance with FFMIA. First, we've been hampered by an old accounting system that does not use the Standard General Ledger; second, our financial statements are not produced directly by our core accounting system; third, our old accounting system does not have the capability to provide cost accounting information in a timely manner; finally, our inspector general has reported that DOT has two material weaknesses, one in FAA's property and another in DOT's information security program.

The first question one might ask is, how did we get into this position? The legacy accounting system in DOT was developed in the 1980's as a single agency accounting system. Over several years in the mid-80's we expanded the system to cover all of DOT. In 1997 we determined that this unique old system could not meet FFMIA and was not cost effective, and we needed to find a new accounting system to meet FFMIA requirements.

In 1998, we selected Oracle Financial—Federal Financials, a commercial off-the-shelf package that has been identified by JFMIP as meeting the Federal accounting requirements. Oracle Financials meet the requirements of FFMIA by providing the ability to use the Standard General Ledger, producing the financial statements as part of the core system, providing the capability to give us cost accounting system information in a timely manner, and having the capability to account for property, plant, and equipment.

We are now about halfway through implementing Oracle department-wide. Within the DOT, we have called this system Delphi. We have about eight agencies up on Delphi right now, and the rest will be completed over the next 11 months. Getting all agencies onto this new financial system will provide a major step toward full compliance with FFMIA. Oracle will largely solve the problems associated with the Standard General Ledger and financial statements. We still face the challenge of providing cost accounting data to our managers.

Three DOT agencies are making good progress in the area of cost accounting. FAA is leading the way in providing accounting data to program officials. They have completed the installation of a cost accounting system covering approximately 75 percent of its cost and expect to have 100 percent of its cost covered by November 2002.

The Coast Guard is also making progress on moving toward cost accounting. At this point, they're able to identify the cost by activity on an annual basis. The newly created TSA, or the Transportation Security Administration, has the advantage of being set up in Oracle with cost accounting from scratch. TSA's cost accounting structure has already been established and a pilot project is under way to capture labor costs at the activity level. Our goal is, for all of DOT agencies, to meet the cost accounting requirements within the next 2 years, and I believe we are on track to accomplish that goal.

We are also addressing the IG's concerns from our 2001 audit. FAA continues to have material weaknesses in its plant, property and equipment. This weakness relates to the proper calculation of the net book value of property held by FAA. The final solution requires that FAA's property accounting system be integrated with the core accounting system. This will occur when FAA moves to Oracle in November 2002.

The IG also noted material weaknesses in our information security program. Regarding our need to certify our financial feeder systems, we have instituted a policy that requires the agencies to have their feeder systems accredited and certified before they can interface with the Oracle system.

Regarding the IG's concerns on our network security and the completion of a background check, this falls under the purview of our Chief Information Officer, and we are actively working with this office and the affected agencies to resolve these items within the next year.

Achieving compliance has been and continues to be a challenge for the Department. We have a plan and we are on track. Upgrading our accounting system addresses many of the system-related issues that have caused us problems in the past.

Implementing changes in the accounting processes that will allow us to take advantage of the cost accounting capabilities in the new system is still a work in progress. I am committed to staying on the path to reach compliance with FFMIA and improving the financial management at the Department of Transportation.

Again, Mr. Chairman I thank you for the opportunity to testify before you, and I would be happy to answer any questions you might have.

Mr. HORN. Thank you very much.

[The prepared statement of Ms. McLean follows:]

STATEMENT OF THE HONORABLE DONNA McLEAN
ASSISTANT SECRETARY FOR BUDGET AND PROGRAMS AND CHIEF FINANCIAL OFFICER
U.S. DEPARTMENT OF TRANSPORTATON
BEFORE THE
COMMITTEE ON GOVERNMENT REFORM
SUBCOMMITTEE ON GOVERNMENT EFFICIENCY, FINANCIAL MANAGEMENT AND INTERGOVERNMENTAL RELATIONS
U.S. HOUSE OF REPRESENTATIVES

JUNE 6, 2002

Mr. Chairman and Members of the Subcommittee:

Thank you for the opportunity to discuss the Department of Transportation's (DOT) progress in achieving the goals of the Federal Financial Management Improvement Act of 1996 (FFMIA). Today, I will present information relevant to the issues your committee has raised on the Department's challenges in trying to become compliant with the FFMIA along with the factors contributing to these challenges and our plan for how DOT will become compliant. First let me clearly state that the DOT is fully committed to achieving the "Standards for Success" for Financial Management as outlined in the President's Management Agenda, and in achieving full compliance with the goals of the FFMIA.

As we have worked to reach this goal, DOT has faced a number of challenges in reaching full compliance with the FFMIA. First, we have been hampered by the existence of a legacy accounting system that is not in compliance with the Standard General Ledger. Second, our Financial Statements are not produced directly by our core legacy system but rather through a financial statements module and a series of spreadsheets. Third, our legacy system does not have the capability to provide cost accounting information in a timely manner to make it useful for daily decision-making. Finally, DOT's Inspector General (IG) has reported that DOT has two material weaknesses: one in the Federal Aviation Administration's (FAA) property, plant and equipment process that resulted in a net book value that could not be substantiated and another in DOT's Information Security Program which has a potential impact on the integrity of DOT financial system.

The first question one might ask is, "How did we get into this position?" The legacy accounting system in DOT was developed in the early 1980's by the FAA to track its accounting data. Through the mid and late 80's this same system was expanded to include all but one of the Department's modal administrations (St. Lawrence Seaway Development Corporation is the only Department agency not using the core system). A decision was made in 1997 that revising the existing legacy system to meet the requirements of FFMIA was not cost effective and an alternative accounting system would be needed to comply with FFMIA requirements. After reviewing the available commercial off-the-shelf software, Oracle Financials was selected as the replacement for the legacy system in 1998. Oracle Financials has been certified by Joint Financial

Management Improvement Program (JFMIP) as an accounting system that meets Federal requirements and we are currently in the process of implementing this new system throughout the entire Department. Within DOT this new system has been named Delphi.

Delphi meets the requirements of the FFMIA and brings to DOT a number of important benefits: it provides the ability to use the Standard General Ledger; it produces the financial statements as a part of the core system; it has the capability to provide cost accounting information to management in a timely way; and it does have the capability to account for property, plant and equipment.

In the early stages of implementation it became clear that the Oracle product would not meet all of DOT's current business requirements without customization. Rather than create customized software we have done two things – in some cases we worked with Oracle to change their program to meet DOT business requirements and in other cases we changed DOT business requirements. This effort has been largely successful to-date. We now have 8 organizations in production on Delphi – the Federal Railroad Administration, the Transportation Administrative Service Center, the Bureau of Transportation Statistics, the Research and Special Programs Administration, the Surface Transportation Board, the Office of the Secretary, the Office of the Inspector General, and the Transportation Security Administration (TSA). Two additional agencies will be converted to Delphi in June – the Federal Transit Administration and the National Highway Traffic Safety Administration. We expect to have the remaining 6 organizations – the United States Coast Guard (USCG), the FAA, the Federal Highway Administration, the Federal Motor Carrier Safety Administration, the Maritime Administration, and the Volpe National Transportation Systems Center – on-line within the next 11 months when full implementation will be complete.

This is an important milestone that will provide a major step towards full compliance with FFMIA. However, although the problems associated with the Standard General Ledger and producing financial statements and other reports in a timely way will be behind us, the challenges that we will still face relate to providing cost accounting data to managers and integration of property and inventory.

Three of the DOT agencies are making good progress in implementing cost accounting – the FAA, the USCG, and the TSA.

FAA is leading the way among the DOT Operating Administrations in providing cost accounting data to program officials. They have completed the installation of a cost accounting system in their largest line of business, Air Traffic Services. In addition, the FAA Academy, the Logistics Center, and the Office of Commercial Space are providing cost accounting data to their managers on a regular basis. These lines of business comprise approximately 75% of FAA funds. Today, FAA is on target to have cost accounting fully implemented throughout the entire agency by November 2002.

The USCG has also made significant progress in implementing Activity Based Cost accounting. However at this time, the USCG has focused on identifying the cost of their activities on a periodic (generally annual) basis. While this produces good information that is useful for budget formulation, the process does not produce timely data for managers to use in their daily decision-making.

The newly created TSA will have the advantage of being set up in Delphi with cost accounting as a requirement from the Agency's inception. TSA's cost accounting structure has already been established and a pilot project is underway to capture labor costs at the activity level.

With respect to the rest of the Department, the remaining agencies on Delphi have not yet started to take advantage of the cost accounting power and capabilities now available to them through full use of the Oracle system capabilities. Our efforts to-date have been targeted towards completing the first step in converting from the legacy system to Delphi and making sure that all current business needs are met. My office is working with each of these agencies to modify their accounting policies and operations so that they can collect data on the full cost of activities and can produce meaningful cost accounting data for managers to use in daily decision making. Our goal is for all DOT agencies to meet the cost accounting requirements within the next two years, and I believe we are on track to accomplish these goals.

DOT is addressing concerns noted by the IG in the areas of property, inventory, and security. As noted in the DOT's IG audit report on DOT's fiscal year 2001 Financial Statements, FAA continues to have a material weakness in their plant, property, and equipment. This weakness relates to the proper calculation of net book value of property held by FAA. The report contained eight recommendations (six from KPMG and two from the IG) which the FAA is in the progress of implementing. The final solution requires that FAA's property accounting system be integrated with the core accounting system. In November 2002, FAA is scheduled to move to Delphi which will automatically calculate net book value of FAA's plant, property and equipment, thereby addressing this material weakness.

The IG's report also noted a material weakness in the DOT's Information Security Program. This weakness is related to accreditation of financial feeder systems, the need to strengthen network security, and the completion of background checks on contractor personnel working on information systems.

As we move to Delphi, we have instituted a policy that requires the agencies to have all feeder systems accredited and certified before they can interface with Delphi. This requires that feeder system operations and processes be documented and approved before they transmit data to Delphi. For some of the older feeder systems, this has been a time consuming effort. We expect all feeder systems to be accredited and certified by May 2003.

The other two security issues, network security and completion of background checks fall under the purview of our Chief Information Officer. We are actively working with his office and the affected agencies to resolve these items within the next year.

Achieving compliance with FFMIA has been and continues to be a challenge at DOT but we are making good progress in achieving our goal of becoming fully compliant. Moving to an accounting system that has been certified by JFMIP addresses many of the system-related issues that have prevented DOT from being FFMIA compliant in the past. Implementing changes in accounting processes that will allow DOT agencies to take advantage of all the new capabilities now available is a work-in-progress. When completed, cost accounting information will be readily available to managers that will provide critical information to them in making business decisions for the operations.

I am confident that we are on the right track to achieving these results. Over the next two years we expect to reach the goal of being fully compliant with the FFMIA and I want to assure you that I am committed to reaching this goal.

Again, Mr. Chairman, thank you for the opportunity to testify before you today. I look forward to responding to any questions you may have.

Mr. HORN. And we'll start on the various questions with Sally Thompson of the General Accounting Office, and let's start with the simple ones.

In your opinion, what it will take for agencies to become compliant with the Federal Financial Management Improvement Act?

Ms. THOMPSON. I think it starts at the top, Mr. Chairman. The Secretary must be committed to reaching success and compliance of FFMIA. They also need to then hold people accountable.

We had thought that one way to do that would be to delegate to their COO the responsibility for reaching success in financial management information. The COO could then pull together a team made up of the CFO, the CIO, program managers, budget people, and the IGs. They could put a master plan together, a roadmap, a blueprint. If you don't have a plan and don't know where you're going, you don't know how to get there. And then that plan could have milestones, good project planning, holding people accountable; then they could report back up to the Secretary, and then it goes up to OMB and to the President.

And we do also feel there needs to be public reporting on this.

Mr. HORN. When you say "public reporting," what do you mean?

Ms. THOMPSON. Well, I think that, again, to continue with the type of oversight hearings that you're having; you know, it's one thing to issue a report, it's another thing to also have a hearing on it and to raise the visibility of the importance.

I think here, over the years, we've been able to determine not only the issues we have over there on the board that have continued, but what you heard today is the importance of cost management information. It's not all about just systems; it's about getting the information—using the information to make decisions.

Mr. HORN. In your study of all this, do you think the person on the level, let's say, below the GS–12, if we're still in that group, do they really take it seriously? Or is this simply for the Assistant Secretaries and the Under Secretaries?

Ms. THOMPSON. It has to be permeated through the agencies, I think. And you know, my background, coming out of the agencies when I was previously a CFO, is that it was a CFO problem. And it was the CFO and maybe the deputy and maybe the person that was head of systems under the CFO. It was never considered a program manager's issue. And that is what I feel needs to—we didn't actively engage the program managers. They are the ones to tell us what information needs to be captured, and then have the CFO and the CIO get the hardware/software together to be able to capture that. I think we need to focus on performance management outcomes and results, how are we going to measure it, where is the data going to come from, how are we going to capture it, and then how do you get it in the system and report it out.

Mr. HORN. In the General Accounting Office document, it's expressed concern that auditors are not doing enough to determine whether agencies really are complying with the Federal Financial Management Improvement Act.

What's the problem and what should be done to correct it?

Ms. THOMPSON. Well, we believe that the act says that both the agency head, as well as the auditor, should report whether an agency is in compliance; and we believe that reporting will require a yes or a no.

What is happening is that for agencies that are compliant, the auditors are saying that nothing came to our attention, which in the auditing standards is "negative assurance," and that means that they didn't necessarily specifically test for all of the compliance of FFMIA.

To do "positive assurance" quite often requires significantly more testing. And we believe that the act says reporting whether that is a yes or a no is positive assurance. We are getting negative assurance.

Mr. HORN. What about OMB, do you—do you ensure any compliance with the FFMIA in your work? How helpful has OMB been?

Ms. THOMPSON. I think that they have put some guidance out there. We do not feel that the processes are rigorous enough for it. And we believe that the agencies and the auditors are interpreting that to say that negative assurance is just fine, that nothing came to our attention; and we believe that if there were positive—if it were interpreted by positive insurance—there would be more rigorous testing on that.

It's not been a big issue right now because, as you know, we only have four agencies that the auditors say that they are complying. But we're hopeful, as the new systems come into place and get implemented, and more data is getting captured, we believe that the auditors need to have a specific audit plan just to look for compliance with FFMIA.

Mr. HORN. The views of the Office of Management and Budget on this issue are very important. Accordingly, the record will remain open for the purposes of including OMB's testimony.

I note that Mark Everson, Comptroller at OMB, will testify before us on the Single Audit Act, and we will question him on this issue as well. He was a breath of fresh air, as far as I was concerned. I hate to see him not have the chance to give us some perspective from a control agency such as OMB.

The few agencies that bother estimating their erroneous payments reported that they improperly spent about $20 billion last year.

How does compliance with the Federal Financial Management Improvement Act relate to improper payments? And is that an accurate figure of $20 billion?

Ms. THOMPSON. Let's start, is that an accurate number.

I do not believe that we know that for sure. The work that the General Accounting Office has done—and I have our Assistant Director, Tom Broderick, here today, who's been in charge of a lot of that work—would tell you that we suspect that it's a lot larger than that. And the reason we don't know, again is because there hasn't been a rigorous process in place for the agencies to really determine what their improper payment total really is.

And we could certainly answer that: Is it a part of FFMIA? I believe it is. We talk about good management information in which to make management decisions. Part of that decision should be to minimize improper payments. So therefore I would consider it a part of FFMIA, even though I think it needs a very specific focus on it.

Mr. HORN. Now, to what degree are the improper payments relevant to the Federal Financial Management Improvement Act?

Ms. THOMPSON. Well, certainly $20 billion that we know, that has been identified, could be very relevant to the Federal Government's management of its resources. I think right there that makes it incredibly important to FFMIA.

I think it goes back to then having the right kind of information to manage from, to make resource allocation decisions. How are we going to know whether a program is achieving results if we don't know that it's going to the right people?

Mr. HORN. We'll get into some of that later—but what should agencies do to reduce these massive overpayments?

Ms. THOMPSON. Can I let our Assistant Director, Mr. Broderick, answer that for you?

Mr. HORN. Certainly.

Mr. BRODERICK. I think there are several things that need to be done to really address the improper payments problem. We issued a report back in October that kind of provided a structure for that.

Essentially what we're looking at is improving internal controls over programs. There's really five areas within that control structure that have to be addressed. We need to make sure that there is a strong control environment over the whole area of improper payments. When we're talking about a control environment, we're talking about establishing a culture of accountability.

We have to make sure that the program managers and the assistant directors or the assistant secretaries and the secretaries and even the people over at OMB understand that this is an important area, understand that we expect results, understand that we expect improvements.

The agencies also have to go through a process which we refer to as risk assessments. Essentially, it's critically important for the agencies to understand if they have problems in their programs, what those problems are, and the extent of those problems. By knowing that information, you can determine where you should focus your efforts, what your high-risk areas are, and you could have a much more logical approach to just focusing on those areas where the problems are, as opposed to a shotgun approach and trying to look at everything in the world, when in fact a whole lot of those efforts might then be useless.

Once you've identified where your problems are, then you have to determine what is the most cost-beneficial or cost-effective way to address those problems. You have to determine the actual actions that you're going to take. And there's a whole laundry list, basically, of the kinds of things that agencies have used. As part of the work that we did, we went to several foreign countries to see what they were doing in some areas where they seemed to have some success. That laundry list includes not only computer kinds of applications and data sharing and different things along that line, but it also gets down to educational activitie—making sure that their people, the agency people, understand the programs, so that when somebody comes in as a beneficiary and says, what do I qualify for, that the agency people ask the right questions and make the right determinations and collect the right information.

We have a lot of problems in some of those areas.

Once the different activities are implemented, then it's also critical that information be fed back to the program managers, the agency management, OMB and the Congress so that they can evaluate and judge what is going on, the progress that is being made in those different areas, so they can establish performance measures and set targets for what the expectations would be for future efforts and for improvement in the future.

In a capsule, those are the general areas where we think the agencies need to focus attention if they are going to address their improper payments problems.

Mr. HORN. I think the General Accounting Office has done a wonderful job on risk assessments. They put out their pamphlets to everybody in the Congress of the new Congress. I'd be curious as to whether the IG, the Inspector General, or the Chief Financial Officer or the Chief Information Officer, should they be the ones to be the oversight within an agency; or how do you look at that?

Or is it—it obviously ought to be the budget—budget people within an agency. Where is the best place to——

Mr. BRODERICK. I think something that Ms. Thompson said a few minutes ago is appropriate here, just as appropriate as it was for FFMIA.

Basically, what we have in the different agencies is, we have program managers, we have CIOs, we have CFOs, we have our IGs, we have a lot of individuals with institutional knowledge, based on the work they do about programs and different kinds of activities and systems. Things that work and don't work.

I think we need a coordinated effort within each of the agencies to pull those people together to try to address the problem areas and come up with solutions, so that you don't just have one group over there trying to figure out what has to be done and what fixes are needed when, in fact, there might be other people who could provide a lot of best-practice kinds of information that might be useful in helping come up with best ways of addressing these problems.

Mr. HORN. Should agencies be required by law to estimate their improper payments?

Mr. BRODERICK. How far do you want me to go on this, Sally?

I think that it's critically important because of the magnitude of improper payments that we're looking at now—and that's just what we know about—that improper payments be reported in a public manner. Certainly legislation is much more binding than any kind of administrative activity or a circular or whatever from the Office of Management and Budget. It would certainly raise the level of interest, I think, at the different agencies that this kind of thing has to be done and that there is interest here.

I think it could certainly be a benefit to have it in legislation, as opposed to possibly some of the other mechanisms that might be put in place to require reporting.

Mr. HORN. Ms. Thompson, it looks like she wants to get her seat.

Mr. BRODERICK. I have no doubt.

Mr. HORN. You're happy—or you can have two or three chairs over there.

Ms. THOMPSON. I would definitely agree with everything Mr. Broderick said, Chairman Horn.

First of all, if you don't measure it, you can't fix it. If it doesn't get reported there, it doesn't have the visibility that it needs to get the problem solved.

Mr. HORN. And you would agree with his answer, I take it, in terms of improper payments and this kind of thing?

Ms. THOMPSON. Absolutely.

Mr. HORN. Later today I will introduce a bill that will require all departments and independent agencies in the executive branch to estimate their erroneous payments. Congress and the administration must understand the scope of this problem before we can find the appropriate means to correct it. We welcome your thoughts on that.

Ms. THOMPSON. Thank you.

I believe that Mr. Broderick has been working with the staff on some issues. I think he identified, first of all, it has to start at the top. It has to create the environment that there is an awareness there, that there is a process for measuring it and, more importantly, a commitment to correct it and to hold accountable people that are going to be working on reducing what we know is the $20 billion and which may be significantly more.

Mr. HORN. Is it right to use "erroneous" or should we use "improper"?

Ms. THOMPSON. We consider the two terms synonymous. OMB, in the President's Management Agenda, has used "erroneous payments." We have used "improper payments" for a long time, so we've continued to do that. But in any public reporting since the President's Management Agenda has come out, we have made it clear that we consider those two terms synonymous. So if you're comfortable with using "erroneous payments," which then ties into the President's Management Agenda, we're fine with that.

Mr. HORN. What I'm thinking about is, if it's really improper, maybe it should be turned over to the U.S. attorney. That's never happened, to my knowledge, when somebody went beyond their budget, I don't think for 100 years anything's been done about it. But there might be such a tremendous amount for one area or one agency or one department, and the question is, if we write into law that's going to be looked at very carefully, what do you mean by that?

Ms. THOMPSON. I think when there's been fraud identified in improper payments, from my background at the Ag Department, those were turned over to the Justice Department. And so I think in that respect, they——

Mr. HORN. Did they ever do anything, the Justice Department?

Ms. THOMPSON. I can't answer that. I didn't followup on it.

Mr. HORN. Did you send it over there to the Department of Justice?

Ms. THOMPSON. There was the starting of investigations when I left.

Mr. HORN. So it's still in, or what?

Ms. THOMPSON. I don't know for sure. I've been gone for a while.

Mr. HORN. Well, they have a lot of big dark corridors and maybe it's passed away in one of those corridors. So, you know, that's fascinating, and we'll try to followup on that.

Ms. THOMPSON. OK.

Mr. HORN. What's the name of the improper activity on that.

Ms. THOMPSON. It would be——

Mr. HORN. Is it a particular case of people or something that happened erroneously?

Ms. THOMPSON. It's been a while, so for the record, I couldn't really state; but we'd be glad to followup on that and see where things are.

Mr. HORN. Well, to quote Connie Chung, maybe "just whisper in my ear."

OK, Karen Alderman, Joint Financial Management Improvement Program. In your testimony, you stated that most financial management systems used by Federal agencies are internally developed products, but that the agencies are rapidly moving to commercial off-the-shelf software. What's been the agency's experience in implementing commercial off-the-shelf software?

Ms. ALDERMAN. I would say there's been a history of change within the software market. Basically, in the 1980's, Core Financial Systems started to be COTS, but they're highly customized commercial off-the-shelf product. What has occurred in more recent history is that the Federal Government has tried to organize the market for COTS more systematically. The JFMIP testing and qualification process is an example of that. The goal is to create a set of capabilities in the commercial off-the-shelf marketplace that meets Federal requirements without customization.

The reason for that is to manage cost and risk. A fully custom designed commercial Core Financial System would cost about $120 million and take 5 years to implement before the first transactions ever pass through the system. A comparable noncustomized COTS product or Core Financial System would take $28 million and 3 years to implement if you can successfully implement it without customization.

We say we're on a continuum.

Success is more than just the software. It's senior leadership commitment to the new system, it is trained staff and capabilities, it is changed management, and it is training of the work force for new systems. So it's more than just software. So there's been improved success, but it's certainly not an easy process today.

Mr. HORN. Does the company that has the off-the-shelf software also have training plans? They've put it all together. Do they provide you with that training or is there something unique here?

Ms. ALDERMAN. I don't think it's a unique process. I think that there are different requirements, system to system; you know, each company presents their products, some are easier to use than others.

But basically, aside from providing some training—the trainer type of service, it is up to the agency to retrain its work force and to implement the business process changes inherent in that product that are necessary to support that product. So it's really an agency responsibility to retrain the work force to support a new system.

Mr. HORN. In my background and reincarnation as a university president, I decided after numerous problems with software/hardware, everything else, that they would—I would always be at the top to get something done, and that's the alpha program. But, frankly, I would never again, and it would be the zebra program, because somebody else can easily try to deal with this problem. And if we can copy what's done in industry in some of this, we ought to take advantage of it, see how it works.

Ms. ALDERMAN. I agree, sir.

But I would also comment that industry has had similar challenges for implementing new systems. Surveys of private industry implementations of enterprise resource programs or large IT projects, only 9 percent come in on time and budget on function. So the government shares the challenge that industry shares with new systems.

Mr. HORN. How many and which agencies currently use systems that have been certified by the Joint Financial Management Improvement Program?

Ms. ALDERMAN. The Core Financial System, which is the only area where we do qualification tests, between 1999 when we started this process and 2006, 20 of the 24 CFO agencies have indicated plans to replace their Core Financial Systems, and virtually all these replacements will be COTS and the COTS will be qualified by the JFMIP functional testing process.

Mr. HORN. Could you elaborate on the system's software qualification process and the impact this process could have on an agency's ability to become compliant with the Joint Financial Management Improvement Program?

Ms. ALDERMAN. Our process includes requirements definition and testing; and what it does is provided assurance at the point of acquisition of software that the software will meet the functional requirements—many of which are critical to FFMIA: That includes general ledger management, funds management, payables management, receivables management, cost management, and reporting.

At the time we started this process, we were a follow-on process to an earlier process which was called a "mandatory FFMS schedule." About 25 percent of Core Financial System Requirements were tested as part of that procurement process. This didn't provide a lot of assurance to the agencies; plus the testing process was—as part of the procurement process, and it wasn't visible to agencies how products were tested.

In 1999 and 2000 incremental tests, we tested about 95 percent of requirements in part or in whole. We have subsequently reviewed all our tests and agency implementations for issues. We've clarified requirements further, added cost requirements, enhanced some areas where we found that the agencies were having difficulties. The follow-on test in 2002 will be even more robust.

So we have raised the bar over time, and all software vendors in this market have had to improve their software. So it provides a step-up, it provides a better tool. But there are still these other issues in implementation that have to be done. Feeder system information, conversion success, training, leadership, all these types of things to be successful in an agency.

Mr. HORN. Can an agency upgrade its certified software without additional approval by the program?

Ms. ALDERMAN. What we do is, we qualify software by version. OMB sets policies that the agency use qualified software. It's our process to just keep versions and agency requirements aligned, and OMB sets the policy.

Mr. HORN. Does GSA have a role in this? They're out there buying products for agencies all over town.

Ms. ALDERMAN. GSA is required to make sure if a vendor that's qualified requests to be on one of their schedules, they will place it on their schedule for the normal process of procurement of schedules.

Mr. HORN. What impact does the poor condition of the financial systems have on the goals of financial management reform legislation?

Ms. ALDERMAN. Which legislation?

Mr. HORN. What impact does the poor condition of financial systems, which seem to be—have on the goals of financial management reform legislation? Is there—is there an impact in that area?

Ms. ALDERMAN. Yes, there is. Basically, agencies have used manual processes to connect all the dots, and that's where they are today; and they will not be able to do that in the accelerated timeframe for financial reporting unless they change their business processes, have more automated systems and less data reentry.

Modern tools are available. It's just the challenge of getting them implemented and supported in the agencies. So it's a critical tool. It's not the whole answer; they're a critical tool.

Mr. HORN. OK, we'll move to one of the key agency members, and that will be Dr. Blanchard, Chief Operating Officer for the Small Business Administration. In your testimony you stated that the Small Business Administration's noncompliance with the Joint Financial Management Improvement Program in fiscal year 2001 caused a slippage on the President's Management Agenda score card from a "yellow" to a "red." What caused the noncompliance?

Mr. BLANCHARD. Yes, sir, we did slip in spite of the improvements in all of the other areas in the financial management arena.

We tried to implement new reporting requirements as per OMB bulletin 01–09. What we wanted to do was try to implement that 1 year early so that we can get a handle on these new requirements. In that process, in trying to wrestle with some of those new requirements. We fell short in terms of timely reporting.

The auditors caught a couple of errors, and they were ultimately corrected. It was that lack of timeliness that created the material weakness and, therefore, automatically downgraded our score in the President's Management Score Card.

Mr. HORN. Well, we all make those mistakes. In your testimony, you stated the SBA has received a clean or unqualified opinion for the past 6 years, yet the SBA did not comply with the Federal Financial Management Improvement Act until fiscal year 2000.

Mr. BLANCHARD. That is correct, sir. I guess the standards for FFMIA compliance are quite a bit different from standards used by the auditing community, and I would say that FFMIA probably has more stringent standards, which are welcomed by this agency, but still present a challenge for us in meeting.

Mr. HORN. The General Accounting Office stated that most agencies do not have timely, accurate, and useful information, including cost data. How useful has the implementation of activity-based costing been for your agency?

Mr. BLANCHARD. Well, it has been very useful. Activity-based costing allows us to determine the full cost of a particular activity. As you know, organizations—public agencies are organized with overhead in support departments and then provide different programs through different program offices, and to determine what the cost of one program is is quite a daunting task, because you have to determine what proportion of the HR function was dedicated to that program and what proportion of the accounting function was dedicated to that program.

So the implementation of that model has helped us very clearly identify the unit costs, so that we can make program cost comparisons and, therefore, measure our performance with that cost component included, and make judgments about budgetary allocations based on those various cost differences and performance differences.

Mr. HORN. Do you believe that other agencies would benefit from using this method of costing?

Mr. BLANCHARD. I do indeed, sir. We have been contacted by other agencies, in fact, asking about how we have implemented and how we have—you know, what type of model we use with regard to the activity-based costing. So it does seem that other agencies are interested.

Mr. HORN. What is the greatest challenge for SBA in becoming compliant with the Federal Financial Management Improvement Act?

Mr. BLANCHARD. I think the greatest challenge for us is really making sure that the automated system, the COTS software, operates properly.

As I mentioned in my testimony, Mr. Chairman, we started early, trying to move in this direction, and procured a software package that predates the software package that is now used by other agencies in the government. Our use of that earlier system has caused us some problems, and we are working to change that.

I have learned, even just today, that some of my colleagues in other agencies have found success with the later release from the same company. So we are—we obviously have pause in going with that related release because of our lack of success in the earlier release, but we are considering options, and they include moving to that more recent package.

Apparently, our problems have been—it is the recent package that is being supported; the earlier package, the support has dropped off. So we are a little disturbed by that and are working with that company to——

Mr. HORN. Join the club.

Mr. BLANCHARD. Well, thank you, sir.

Mr. HORN. It is a long club, starting with me.

Mr. BLANCHARD. But I think for us, the keys of compliance that were mentioned by Ms. Thompson earlier, including senior management leadership with regard to delegating budgetary and financial responsibility to the chief operating officer are something we have already achieved at SBA. I am the lead person on financial matters at the agency, and of course we do engage in cost information management and the public reporting that Ms. Thompson also referred to. So we feel like it is just the implementation of the COTS package that prevents us from being compliant.

Mr. HORN. Well, Ms. McLean, I have a couple of questions for you, and then I think we will move on.

What are the greatest challenges for the Department of Transportation in being compliant with the Federal Financial Management Improvement Act?

Ms. MCLEAN. Well, as Dr. Blanchard mentioned, just the transition to a new financial system has been a big challenge, and it will be a 5-year effort, once we are finished. Again, even though we are using the Oracle off-the-shelf package, these systems often were designed really for the private sector and then sort of forced into a Federal package. And so when we are the first ones out of the box trying to put it in place, you end up sort of spilling blood for the folks who are going to come behind you. But that would have been the case in any of the packages we would have taken.

So, luckily, I think with the new module we have, 11, which is the Oracle package we are using, it is dealing with a lot of the issues we had previously with Oracle.

I think the second challenge we are going to have is the cost accounting piece, and, in fact, not just creating and collecting the cost accounting data, but training our managers so they actually use it and make decisions on those—based on that information.

Mr. HORN. In your testimony, you stated the Department of Transportation is expected to be in compliance with the Federal—whatever that thing is, you know, I hate these initials; they drive me nuts—Federal Financial Management Improvement Act, in the next 2 years.

Ms. MCLEAN. Yes, sir.

Mr. HORN. How realistic is this 2-year timeframe?

Ms. MCLEAN. Well, I think it is quite realistic, because again, we are in the last stretches of implementing Oracle for our financial—our accounting system, and we should have that done in the next 11 months. And then the cost accounting systems, our biggest agencies within the Department—FAA, Coast Guard, and the Transportation Security Administration—are either finished or well on their way to finishing their cost accounting system. So what we have to finish in 2 years is actually our smaller agencies to come-up on cost accounting.

Mr. HORN. Now, has that program—has that been across the whole department? Because I remember in the last 10 years with the FAA, and it was chaos.

Ms. MCLEAN. For cost accounting?

Mr. HORN. I do not know if it was for cost accounting, but it was just—I knew when I walked in the room, these people do not know what they are doing, and I was right. It turns out that, first, it was $4 billion, then it was $12 billion, then it was $40 billion, and finally, somebody had the guts to pull the plug.

So where are we with the FAA in relation to the Department of Transportation?

Ms. MCLEAN. Well, regarding the FAA's accounting systems, in their cost accounting system, FAA had a—there was an aviation law passed, I believe—in 1996, I think—that required FAA to have a cost accounting system, and that was running ahead of when the

Department was planning to implement an accounting system, the new accounting system. So FAA actually has Peoplesoft for their cost accounting system. They had to develop that at the same time they were transitioning to a new accounting system.

So it has been a huge challenge for FAA, but I really think we are coming to the end of that, because we do have FAA, right now, using cost accounting information to make decisions.

I know you don't have a lot of time, but I can give you some examples if you have some time.

Mr. HORN. That is fine. If you want to add some more, we will put it at this point in the record.

Ms. MCLEAN. Certainly.

Mr. HORN. What is the Department of Transportation doing to address computer security weaknesses, and do you have a lot of hackers trying to get into your systems?

Ms. MCLEAN. Regarding our accounting systems, I know we have not had—we are fortunate enough not to have had many attempts to get into the system. But Oracle is an Internet-based system, so we are taking a lot of precautions to make sure that the security is in place and; as I mentioned, all of the feeder systems, we have 25 financial feeder systems that have to go into Oracle. They must all be certified before we turn on the Oracle financials.

I think it is something we are going to have to just continually watch.

Mr. HORN. It has been 6 years since the passage of the Federal Financial Management Improvement Act. Is there any legislative action—is there any legislative action that Congress should consider to refine or modify the requirements of the act? What do you think?

Ms. MCLEAN. I think one of the things that—and this is a big one, so I do not think necessarily this will be adopted. But one of, I think, the problems with the time it takes the Department to, in fact, implement a cost accounting system is because the appropriations that are passed for the agencies tend to be in buckets of people, capital, grants. You know, you have different accounts; that money cannot be blended or moved between those accounts. So our Appropriations Committee basically identifies money in these pots. Of course, the philosophy——

Mr. HORN. Do you have reprogramming authority?

Ms. MCLEAN. We do not, not within those specific accounts. We do within the accounts, but not between them.

So then you have the philosophy of cost accounting, which of course is absolutely the opposite of this accounting approach, which is, let's see the fully loaded cost. So in the case of DOT, what is the cost of providing search and rescue for the Coast Guard? We have to pull the money out of the people account—I mean the appropriations account; you have to pull the capital money out from the appropriations account, you have to pull the benefits out of that account, and you have to have basically two systems, one system to manage it because the law requires you to have your appropriations by these specific accounts, and then another system over top that pulls the information for cost accounting purposes. So this is a big one.

But if we had accounting—or if our Appropriations Committee had more service-based appropriations, I think we would have a quicker leap from accounting system to cost accounting, and it would cause, I think, managers to think more holistically of what is my budget, not just my pieces.

Mr. HORN. Yes. Forty years ago, all they thought in House Appropriations, how many people do you have, etc. And we got through that, and we have programmatic approaches. That was helped by GAO, where until Mr. Rayburn died and Mr. Cannon, Clarence Cannon, head of Appropriations, died; at last, they could have what we had put on the books in 1946 to look at things in a programmatic way. GAO has done a wonderful job of looking at that.

Obviously, if there are problems here, we ought to—we would welcome the—which we should deal with. You are the people that have to do that every day, and you probably say, what idiot put this in?

Ms. MCLEAN. No, sir, we do not say that.

Mr. HORN. I will not tell you that if I find the idiot, I will say that you led me there. But just to give us some, either on plain paper or anything else, but we will put it in the right place. We ought to do that.

Do not be scared. In Congress, we are trying to get things done.

So I would like to know, do others have a feeling here that we ought to modify the requirements of the act? Any thoughts on that?

Ms. ALDERMAN. I think that there is a big challenge just to get to the current level. I think that the appropriations full cost visibility is a big challenge. It might be possible with technology, but there is a mindSet that would have to be overcome. It is not just technology, it is a mind set, and I think Congress does set that mindset in the appropriations process.

Ms. THOMPSON. Culture.

Ms. ALDERMAN. Culture.

Mr. HORN. Dr. Blanchard.

Mr. BLANCHARD. I would agree with Ms. McLean and others. The appropriations mechanism does create a challenge for the kinds of accounting that are required of us today. There are ways to overcome that, but they are difficult, and many have yet to figure that out.

We have been successful through developing crosswalks which simply communicate between the two systems, in effect, building a patch between the two systems. But it is an evolutionary process as everything changes. So I would think that the requirements that we face today would benefit from some change in the appropriations structure.

Mr. HORN. I think you are right. And when I testified 25 years ago, I think we were moving ahead, and a lot of things have happened since those days.

I would like to thank each one of you, and I want to thank the staff of both the majority and the minority behind me: Mr. Russell George, the staff director and chief counsel; Bonnie Heald is the deputy staff director; Henry Wray is here, who is the senior counsel; Rosa Harris to my left and your right is a General Accounting Office detailee and is on loan to us, and she has done a tremendous job, and we thank her profusely; Justin Paulhamus is our majority clerk; Chris Barkley, a new subcommittee staff member; Michael Sazonov, subcommittee intern, Sterling Bentley, also a new subcommittee intern.

And the minority staff: David McMillen, a professional staff member; and Jean Gosa, minority clerk. We thank you. And the court reporters are Julie Thomas and Julie Bryan, and we thank both of you.

With that, we are adjourned, and thank you.

[Whereupon, at 11:35 a.m., the subcommittee was adjourned.]

[The prepared statements of Hon. John Sullivan and Hon. Janice D. Schakowsky follow:]

Opening Statement
Government Efficiency, Financial Management, and Intergovernmental Relations Subcommittee Hearing on "The Federal Financial Management Improvement Act of 1996: Are Agencies Meeting the Challenge?"
Congressman John Sullivan
Thursday, June 6, 2002

Mr. Chairman, I appreciate the opportunity to address the Subcommittee for the first time. As the newest Member of the Subcommittee, I am looking forward to this hearing and to working on the Subcommittee. It is an honor to be a part of this distinguished body and I look forward to making sure that our taxpayer's money is being spent efficiently, and that Congress is doing everything it can to help the federal agencies with their tasks.

STATEMENT OF THE HONORABLE JAN SCHAKOWSKY
AT THE HEARING ON
THE FEDERAL FINANCIAL MANAGEMENT IMPROVEMENT ACT

JUNE 6, 2002

Thank you Mr. Chairman. Today's hearing tells the story of aging systems and scarce resources for replacing and modernizing those systems. This is, to some extent understandable. We pay far more attention to the results of agency actions than to the management of those actions. In a period of scarce resources, however, the quality of management is more important than ever. Without the proper information to manage, good management is more a mater of luck than planning.

The testimony today from the Department of Transportation is an excellent example of how an agency, with proper leadership, can move towards better financial management. Secretary Mineta is to be commended for his leadership of the Department. This testimony also shows how difficult it is to move an established department from one style of management to another.

We should not be surprised that many agencies have yet to come into compliance with the Financial Management Act. It has taken most agencies a number of years to get to the point of producing a set of books that can be audited. With those books in place, they agencies now have a road map for fixing the systems that feed into those accounts.

We should be surprised, however, if we do not begin to see improvement soon. It is likely that the agencies that do not come into compliance over the next five years, are not investing in the appropriate management tools.

Changing systems is no easy task. We only have to look to the District of Columbia's department of motor vehicles to see how disastrous such a change can be. I don't think we want a situation where improving the financial management system results in a degradation of services. Agency heads must put serving the public first, and fixing the systems second.

I thank the witnesses for taking the time to appear before us today.