

**The Integrated Financial System Software  
Does Not Comply With Some Accounting  
Standards or Contain Certain Functionality as  
Originally Asserted by the Vendor**

**September 2004**

**Reference Number: 2004-10-187**

**This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.**



DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

INSPECTOR GENERAL  
for TAX  
ADMINISTRATION

September 23, 2004

MEMORANDUM FOR CHIEF FINANCIAL OFFICER

*Gordon C. Milbourn III*

FROM: Gordon C. Milbourn III  
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report – The Integrated Financial System Software Does Not Comply With Some Accounting Standards or Contain Certain Functionality as Originally Asserted by the Vendor (Audit # 200410003)

This report presents the results of our review of the Internal Revenue Service's (IRS) planned Integrated Financial System (IFS). The overall objective of this review was to determine whether the IFS, when implemented, would function as intended to provide administrative financial management information that is essential for financial statement preparation and useful to IRS managers and others.

The implementation of the proposed IFS will greatly affect the way the IRS records and reports both administrative and custodial accounting transactions. Further, this system represents a key element of the corrective actions being taken by the IRS to ensure its accounting system is in compliance with the Joint Financial Management Improvement Program's (JFMIP)<sup>1</sup> *Federal Financial Management System Requirements*, and provides accurate and timely financial information for management decision making.

In summary, we determined that the IFS may be at risk of being noncompliant with Federal Financial Management Improvement Act of 1996 (FFMIA)<sup>2</sup> requirements. The IFS either does not include functionality required by various accounting standards or has had workarounds initiated by the IRS to compensate for the nonfunctionality. Further, the IRS needs to take a coordinated and united stance when negotiating any costs with the contractor over asserted "Out of the Box" requirements that are not met

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<sup>1</sup> The JFMIP is a joint undertaking of the United States Department of the Treasury, the Government Accountability Office (formerly the General Accounting Office), the Office of Management and Budget, and the Office of Personnel Management working in cooperation with each other and other agencies to improve financial management practices in the Federal Government.

<sup>2</sup> Pub. L. No. 104-208, 110 Stat. 3009.

by the vendor's software. We also identified that contractor-performed data conversion efforts are progressing, including evaluations being made by an independent IRS validation team to ensure the converted data was accurately recorded. Finally, progress has been made on a previously reported Treasury Inspector General for Tax Administration finding to ensure that all JFMIP requirements are addressed in the system's design.

We recommended the Chief Financial Officer (CFO) ensure that all JFMIP and FFMI requirements and accounting standards are operating before the IFS deployment. If this is not feasible, the IRS should move to the government version of the IFS as soon as possible, and the CFO should ensure that these requirements are included in that version. We also recommended the CFO, in concert with the Director of Procurement and the Associate Chief Information Officer, Business Systems Modernization, ensure a coordinated and united stance is taken when conducting negotiations with the IFS contractor concerning the costs associated with the functionality of accounting requirements that were asserted to be ready for deployment by the software subcontractor. These officials should also ensure all costs are considered when any negotiations are held concerning system requirement deferrals. Finally, we recommended that the CFO ensure that all JFMIP requirements not originally included in the IFS' System Requirements Report are added to subsequent versions of the report and are included in future IFS releases.

Management's Response: IRS management agreed with our recommendations. The CFO will ensure those requirements not satisfied in the IFS Release 1 are implemented in subsequent enhancements or upgrades. Upon successful implementation of the IFS Release 1, the CFO will develop an action plan to address enhancements and future releases of the IFS – especially the upgrade to the Federal Government version of the software, which should close many of the existing JFMIP gaps. Additionally, the CFO has implemented the recommendation to coordinate the IFS contract negotiations with the Director, Procurement, and the Associate Chief Information Officer, Business Systems Modernization, and has worked together to ensure all costs associated with the requirements that were asserted to be ready for deployment by the software subcontractor, but not delivered in Release 1, were included in the negotiations. The IRS' current contract is a cost-sharing contract where the IRS is responsible for 24 percent of the costs and the contractor is absorbing 76 percent of the costs incurred from May 1, 2004, through January 31, 2005. Management's complete response to the draft report is included as Appendix IV.

Office of Audit Comment: The IRS, when acquiring subsequent releases of the IFS containing the requirements that were asserted by the subcontractor to be functional in Release 1, should take into consideration any significant deviations from the concessions received during the recent negotiations when estimating or accepting a price for those future releases.

Copies of this report are also being sent to the managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Daniel R. Devlin, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organization Programs), at (202) 622-8500

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### Background

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The Internal Revenue Service (IRS) is in the midst of Business Systems Modernization (BSM), a major technological and business process transformation program. The BSM will radically change the IRS' approach to satisfying its customers – the taxpayers.

To achieve legislative compliance and provide critical financial management information, the IRS acquired, through contractor assistance, a commercial-off-the-shelf software package, designated as the Integrated Financial System (IFS), as a cost-effective alternative to improve its financial systems. The implementation of the proposed IFS will greatly affect the way the IRS records and reports both administrative and custodial accounting transactions. In addition, the development of the IFS supports one of the President's Management Agenda initiatives to improve financial performance, which involves ensuring Federal Government financial systems produce accurate and timely financial information for management decision making.

One basic, yet significant, requirement of the IFS is that the system is to be compliant with the Joint Financial Management Improvement Program's (JFMIP)<sup>1</sup> *Federal Financial Management System Requirements*.<sup>2</sup> The IRS also expects the IFS to resolve several longstanding financial management issues, including the compliance with JFMIP requirements, identified by the Government Accountability Office (GAO) during the annual financial statement audits.

The IRS plans to implement the IFS in a series of releases over a period of several years. Release 1 will include the JFMIP core accounting functions of Accounts Payable, Accounts Receivable, General Ledger Management, Budget

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<sup>1</sup> The JFMIP is a joint undertaking of the United States Department of the Treasury, the Government Accountability Office (formerly the General Accounting Office), the Office of Management and Budget, and the Office of Personnel Management working in cooperation with each other and other agencies to improve financial management practices in the Federal Government.

<sup>2</sup> The Federal Financial Management System Requirements are a series of publications prepared by the JFMIP as the key requirements that agency systems must meet to be substantially compliant with generally accepted accounting principles for the Federal Government.

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Execution, Cost Management (also referred to as Cost Accounting), and Financial Reporting, as well as Budget Formulation. Release 1 will also include the mandated Health Coverage Tax Credit functionality. Subsequent releases will provide for additional financial management functions, including Property and Procurement Management, and enhancements to the cost accounting and finance modules. However, these future releases and enhancements are on hold and are currently unfunded.

To increase the probability that the IFS will function as intended and meet defined requirements, the IRS is working with a contractor to conduct system testing prior to deploying the IFS. System testing is an essential component of the Enterprise Life Cycle, which governs system development activities and is required by IRS procedures.

This online audit is a follow-on review to our two prior audits. In the first audit report, issued in August 2003,<sup>3</sup> we reported on IFS requirements definition. In the second audit report, issued in March 2004,<sup>4</sup> we reported on IRS' IFS phase I system-testing efforts. In addition, the Treasury Inspector General for Tax Administration (TIGTA) Information Systems Programs audit staff, who are responsible for evaluating systems modernization from an information technology perspective, have previously issued a report containing concerns about IFS testing.<sup>5</sup>

This review was performed at the IRS National Headquarters in the office of the Chief Financial Officer (CFO) located in Washington, D.C., and the contractor's testing site located in Lanham, Maryland, during the period November 2003 through July 2004. The audit was conducted in accordance with *Government Auditing Standards*. Our ability to totally accomplish our audit objective as initially envisioned was limited in that we

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<sup>3</sup> *Requirements Definition of the Integrated Financial System* (Reference Number 2003-10-179, dated August 2003).

<sup>4</sup> *Improvements Are Needed for Subsequent Integrated Financial System Testing* (Reference Number 2004-10-052, dated March 2004).

<sup>5</sup> *Risks Are Mounting as the Integrated Financial System Project Team Strives to Meet an Aggressive Implementation Date* (Reference Number 2004-20-001, dated October 2003).

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encountered situations beyond our control that affected our testing scope. Detailed information on our audit objective, scope, and methodology (including certain audit scope limitations encountered during the audit) is presented in Appendix I. Major contributors to the report are listed in Appendix II.

This audit was conducted while changes were being made to both IFS system design and business process procedures. Any system design or business process changes that have occurred since we concluded our analyses are not reflected in this report.

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**Risk of Noncompliance With the  
Federal Financial Management  
Improvement Act of 1996**

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The Federal Financial Management Improvement Act of 1996 (FFMIA)<sup>6</sup> establishes in statute certain financial management systems requirements that were already established by Executive Branch policies. The FFMIA was intended to advance Federal Government financial management by ensuring that Federal management systems can and do provide reliable, consistent disclosure of financial data. Further, this disclosure should be done on a basis that is uniform across the Federal Government from year to year by consistently using professionally accepted accounting standards. Specifically, FFMIA § 803 (a) requires each agency to implement and maintain systems that comply substantially with:

- Federal Government financial management system requirements.
- Applicable Federal Government accounting standards.
- The Government Standard General Ledger at the transaction level.

The *Federal Financial Management System Requirements* are a series of publications prepared by the JFMIP as the key requirements that agency systems must meet to be substantially compliant with generally accepted accounting principles for the Federal Government.

In the last several years, the GAO has reported numerous financial management weaknesses in its audits of the IRS

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<sup>6</sup> Pub. L. No. 104-208, 110 Stat. 3009.



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annual financial statements and related assessments of internal control. The IRS has proposed the IFS as the remedy for administrative financial management weaknesses.

As a result of our analysis and observations performed with responsible CFO staff, numerous concerns were identified during system testing. We believe these concerns may put the IRS at risk of being noncompliant with FFMIA requirements. Specifically:

- The IFS Status of Funds Report that shows the budget, commitments, obligations, expenditures, and available budget balance at each level and sublevel of the IRS does not roll up to reflect an accurate status of funds needed for executive management's day-to-day decision making. The IRS identified this condition during system testing and is working with the vendor to correct the situation. The JFMIP requires that the core financial system provide complete, reliable, consistent, timely, and useful financial management information on operations to enable individual operating components, divisions, bureaus, and other subunits to carry out their fiduciary responsibilities; deter fraud, waste, and abuse of resources; and facilitate efficient and effective delivery of programs by relating financial consequences to program performance.
- The IFS cannot produce the Statement of Net Cost in accordance with Office of Management and Budget (OMB) Bulletin No. 97-01, *Form and Content of Agency Financial Statements*, because the system is currently unable to split costs between Federal and non-Federal entities. The IRS is working with the vendor and hopes to correct the situation by January 2005. If they are unable to do so, the IRS will need to initiate a workaround to deal with the situation. The JFMIP requires that the financial system facilitate the preparation of financial statements and other financial reports in accordance with Federal accounting and reporting standards.

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- The cost accounting module of the IFS, envisioned for implementation in October 2004, will not accumulate full cost for major IRS programs, reimbursable work, or chargeable user fees as required in the Federal Accounting Standards Advisory Board's Statement of Federal Financial Accounting Standard No. 4, *Managerial Cost Accounting Concepts and Standards*, and OMB Circular No. A-25, *User Charges*. At this time, the system has the capability, but the IRS does not or at times can not collect detailed programmatic information from feeder systems to support full costing. The system envisioned for implementation will accumulate fully burdened cost at an activity level based on payroll codes, which is an improvement over the current system. Although we agree that this is a significant first step in developing a viable cost accounting system, we do not believe the IRS will rectify longstanding GAO and TIGTA recommendations or meet JFMIP mandatory requirements when the IFS is implemented. A cost accounting system should provide the data needed for accountability over the financial execution of public programs; meaningful comparisons to measure compliance with management policies; evaluations of the efficiency and economy of resources used in the various activities; and support for fees, services, or products.
- The IFS does not have the capability to display an overrideable error message when attempting to post previously unrecorded obligations relative to expired funds during the current year as required by JFMIP core requirements. The system as initially configured prevented the posting of new requisitions and obligations using expired funds. Additionally, the system was configured to prevent the posting of an obligation without a requisition for current and expired funds. The IRS chose as a workaround to reconfigure the system to allow new obligations against expired funds and to control this functionality through system user authorization

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levels. Five employees will be authorized to obligate funds without a requisition posted in the system. Although this workaround may solve the situation, it increases the risk that unauthorized obligations can be recorded in the system without a previously posted requisition.

- The IFS cannot accurately produce individual or consolidated Wage and Tax Statements (Form W-2) for employees who incur taxable income involving multiple state tax withholdings. The system can only produce multiple Forms W-2 with each one showing the employee's individual state tax withholding, but showing total taxable income on each Form. This condition could cause employees to overstate their Federal income, if they follow tax-reporting instructions that state, in general, to enter all income amounts on their Federal tax return shown on each Form W-2 received. The IRS identified this condition during system testing and has informed the vendor of the situation. The vendor informed the IRS that a solution will be provided with its release of tax updates in November 2004. If the update is not provided timely, the IRS has planned for compensating controls outside of the IFS to correct this situation.

In addition to the conditions identified during our detailed audit tests, the IRS informed us that as of May 21, 2004, 142 JFMIP requirements are being moved to future IFS releases due primarily to the fact that the IFS version the IRS acquired was geared to commercial use and would have been too expensive to re-fit for government use. Further, a majority of the moved requirements should be met by the currently existing government version of the IFS. Examples of requirements not fully functional in the commercial version of the IFS include the ability of the system to record full or partial receipt and acceptance of goods and services by line item and the ability to indicate if a payment is partial or final. Also, the commercial version is not able to meet the requirement to maintain accounts for reimbursable orders and identify government and nongovernment accounts that are designated as advance funding.

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Further, the IRS has identified five JFMIP requirements needing implementation as soon as possible. Three of these five pertain to the preparation of the Statement of Net Cost. The IRS is working with the contractor to obtain the needed functionality of these requirements in future module releases and system upgrades.

**Recommendation**

1. The CFO should ensure all JFMIP and FFMIA requirements and accounting standards are operating before the IFS deployment. If this is not feasible, the IRS should move to the government version of the IFS as soon as possible, and the CFO should ensure these requirements are included in that version.

Management's Response: Given the time scheduled for implementation and the complexity of the project, the CFO did everything possible to ensure relevant JFMIP and FFMIA requirements and accounting standards were delivered in Release 1 of the IFS. The CFO will ensure those requirements not satisfied in Release 1 are implemented in subsequent enhancements or upgrades. However, as indicated in the report, subsequent planned releases of the IFS have been put on hold due to the current IRS funding situation. Upon successful implementation of the IFS Release 1, the CFO will develop an action plan to address enhancements and future releases of the IFS – especially the upgrade to the Federal Government version of the software which should close many of the existing JFMIP gaps.

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**Asserted Out of the Box  
Requirements Were Not Met by  
Vendor Software**

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During system integration and configuration, the IRS identified 531 functional requirements, as of May 21, 2004, that were not met by the IFS. These requirements are being either deferred to future IFS releases or designated as needing immediate attention. Of these 531 requirements not met, 473 were asserted by the IFS software subcontractor as being met “Out of the Box.”

Section C of Task Order (TO) number 0091 of the IRS' implementation contract related to the preliminary development of the IFS states in general, under the

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*Performance Based Work Statement Matrix* heading of *Performance Standard*, that the system design meets 100 percent of selected requirements as asserted by the software subcontractor as “Out of the Box.” Section C, Performance Standard Number four defines “Out of the Box” requirements as those that would be met by means of configuration only and the requirement would be met without modifying code or making database changes that would add time, effort, or complexity to upgrades.

Section G, item H.7, goes on to state that any differential costs associated with approved deviations from the performance standard to meet 100 percent of selected requirements “Out of the Box” would be borne by the software subcontractor and are unallowable costs under the TO. Differential costs are defined as any costs over and above the costs to meet the requirements through configuration.

Because of system requirement deferrals, the IRS is forced to develop workarounds to ensure accounting standards are met when the system is deployed. For example, the IFS does not meet the system requirement to provide the capability to automatically offset payments to vendors based on current outstanding receivables. In another example, the IFS does not have the capability to split an invoice into multiple payments on the appropriate due dates when items on the invoice have different due dates or discount terms.

Per the IRS, as of June 30, 2004, approximately \$137.8 million has been obligated for IFS implementation TOs and other obligations, with the IRS recording expenditures of approximately \$121.1 million against those obligations. Of those amounts, approximately \$113.8 million and \$98.3 million represent obligations and expenditures, respectively, to the IFS vendor. These amounts only include external costs and do not include costs incurred for IRS personnel or resources.

We understand negotiations were recently completed to deal with the issue of deferred requirements that were asserted by the software subcontractor as “Out of the Box” and an amendment to the relevant TO was signed on July 15, 2004. Notwithstanding these recent negotiations, we believe IRS

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resources are at risk if it does not take a coordinated and firm stance when dealing with the vendor when it pertains to the delivery of system requirements (i.e., the participation of the CFO, Chief Information Officer (CIO), and Procurement staffs, as needed, to ensure that system implementation, accounting functionality, and acquisition regulation concerns are jointly represented and presented). Also, if further negotiations are required, the IRS needs to consider not only the cost to implement any further deferred requirements, which would represent unallowable costs under the contract, but to also consider the financial impact of IRS resources needed to identify and ensure the ultimate implementation of the requirements into the IFS. These costs should also include the cost of workarounds needed to ensure IRS systems meet accounting standards.

### **Recommendations**

The CFO, in concert with the Director of Procurement and the Associate CIO, Business Systems Modernization, should:

2. Ensure a coordinated and united stance is taken when conducting any negotiations with the IFS contractor concerning the cost associated with the functionality of accounting requirements that were asserted to be ready for deployment by the software subcontractor.

Management's Response: The CFO has implemented the recommendation to coordinate the IFS contract negotiations with the Director, Procurement, and the Associate CIO, Business Systems Modernization.

3. Ensure all costs are considered when any negotiations are held concerning system requirement deferrals.

Management's Response: As recommended, the IRS has worked together to ensure all costs associated with requirements that were asserted to be ready for deployment by the software subcontractor, but not delivered in Release 1, were included in the negotiations. The IRS' current contract is a cost-sharing contract where the IRS is responsible for 24 percent of the costs and the contractor is

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absorbing 76 percent of the costs incurred from May 1, 2004, through January 31, 2005.

Office of Audit Comment: The IRS, when acquiring subsequent releases of the IFS containing the requirements that were asserted by the subcontractor to be functional in Release 1, should take into consideration any significant deviations from the concessions received during the recent negotiations when estimating or accepting a price for those future releases.

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**Data Conversion Efforts Are  
Progressing**

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The JFMIP has stated that of the many critical tasks necessary to successfully implement a new financial system, data conversion<sup>7</sup> is one of the most frequently underestimated. From the outset, it should be understood that financial systems data conversion is a complex and difficult task that requires highly skilled staff to conduct successfully. If data conversion is done right, the new system has the opportunity for success. The JFMIP concludes by stating that converting data incorrectly has lengthy and long-term repercussions.

The IRS' contractor has developed a Data Conversion Test Plan describing procedures to execute and document the unit testing of all data conversion components, followed by comprehensive end-to-end testing via mock data conversion cycles.

Unit testing includes validating that each conversion program for a given component performs according to the technical specifications and expected results are documented in the test scripts. The mock conversion tests test the full data conversion life cycle and are executed before the production cutover is performed to ensure that the timing of the conversion is as short as possible and that all data anomalies have been addressed.

Finally, test scripts were created to support the unit testing of each conversion component, as well as the mock conversions. The scripts include expected results for each test. During test execution, if a conversion is not successful

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<sup>7</sup> Data conversion is the modification of existing data to enable it to operate with similar functional capability in a different environment.

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because of a flaw in the functional design of the conversion or a flaw in the conversion program, a defect report is logged and tracked until the conversion of the component is successful.

The primary sources of legacy data are the Automated Financial System,<sup>8</sup> the Budget Formulation System/Plan Development System, and the Requisition Tracking System/Integrated Procurement System. The primary targets include various financial components of the IFS software and the Strategic Enterprise Management/Business Warehouse component. The conversion teams will utilize both manual and automated conversion methods to accomplish their tasks.

The contractor, along with the IRS, has developed selection criteria and validation methods for all the components of data conversion. Additionally, the IRS has formed a team to independently validate all converted information using their own validation tools and acceptance criteria.

As of July 21, 2004, the IFS data conversion's first two mock cycles failed because the system's environment was constantly changing. The third cycle was completed and the year-end closing of accounts was demonstrated, but some problems were encountered that still need to be resolved. The IRS' validation team is currently evaluating the results of the third mock conversion cycle to ensure all data were accurately recorded. A future data conversion cycle is planned after all changes to the process have been implemented. The IRS will use this cycle to determine if all system changes were successfully implemented and to approximate how long the conversion process will take when the system is implemented.

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<sup>8</sup> A computer-based financial accounting system used by the IRS to track appropriations and expenditures.



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**Progress Has Been Made to  
Ensure All Joint Financial  
Management Improvement  
Program Requirements Are  
Addressed**

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In a prior TIGTA audit report<sup>9</sup> concerning IFS requirements definition, we reported that the IRS established a framework to identify material administrative accounting requirements for inclusion in the IFS. However, we did identify 64 JFMIP requirements that were not specifically or fully addressed in the IFS' System Requirements Report (SRR), which represents the detailed design of the IFS. Of these 64 requirements, 36 represented mandatory JFMIP requirements and 28 represented value-added requirements.

We recommended that the Acting CFO, along with the IFS contractor, ensure that the identified JFMIP requirements were fully addressed and incorporated into the IFS' SRR.

In management's response, CFO officials stated they had assessed the missing or incomplete JFMIP requirements included in the report and provided assurances that the requirements either are addressed through a collection of requirements in the SRR or will be addressed by ensuring that the requirements are included in future releases of the IFS.

Of the 36 JFMIP mandatory requirements, we agree the IRS has addressed 30 of the requirements, and that 2 requirements are not valid for IRS' business processes. The remaining four requirements, which pertain to the property and travel modules, are to be addressed in future releases of the IFS. Since these modules are not yet formulated or the IRS has not initiated related change requests on them, we were unable to assess whether these requirements were added to the IFS' SRR.

For the 28 value-added requirements, we agree the IRS has addressed 7 of the requirements. The remaining 21 requirements, which mostly pertain to the property, travel, and seized assets management modules, are to be addressed in future releases of the IFS. As with the mandatory requirements being addressed in future releases, we were unable to assess whether these requirements were added to the IFS' SRR. Although the IRS is not mandated to implement value-added requirements, we believe the IRS

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<sup>9</sup> *Requirements Definition of the Integrated Financial System* (Reference Number 2003-10-179, dated August 2003).

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should continue to assess the requirements when designing future releases.

**Recommendation**

4. The CFO should ensure the remaining JFMIP requirements are added to subsequent versions of the SRR and are included in future IFS releases.

Management's Response: The CFO will ensure any requirements not satisfied in Release 1 are identified and implemented in subsequent enhancements or upgrades. However, as indicated in the report, subsequent planned releases of the IFS have been put on hold due to the current IRS funding situation. Upon successful implementation of the IFS Release 1, the CFO will develop an action plan to address enhancements and future releases of the IFS – especially the upgrade to the Federal Government version of the software which should close many of the existing JFMIP gaps.

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**Appendix I**

**Detailed Objective, Scope, and Methodology**

The overall objective of this review was to determine whether the Integrated Financial System (IFS), when implemented, would function as intended to provide administrative financial management information that is essential for financial statement preparation and useful to Internal Revenue Service managers and others. To accomplish this objective, we:

- I. Verified that IFS financial system requirements and related internal controls were effectively identified and tested and would deliver an integrated financial system that meets established financial requirements when implemented.
  - A. Reviewed IFS general ledger posting guidance for consistency with established Office of Management and Budget guidance, legislative mandates, and Federal accounting standards.
  - B. Reviewed System Integration Testing – 2 (Release 1) procedures and plans to gain an understanding of the testing process.
  - C. Judgmentally selected 164 of approximately 2,900 system requirements based on 9 accounting functional areas<sup>1</sup> that we believed, if validated, would provide a basis to reach conclusions about the overall functionality of the IFS. The 164 system requirements affected 58 test cases that we attempted to analyze. Our planned analysis involved review of the test case, observation of the actual test, review of post-test supporting documentation, and discussions with subject matter experts concerning the test results.
  - D. Of the selected 58 test cases, we were able to review 53 test cases for reasonableness and ability to exhibit the functionality of the affected system requirement. Four test cases were found to be deleted and one was a duplication of another test case. However, due to initial untimely notification of test scheduling, we were only able to observe 29 of the selected 58 test cases. Further, we were only provided 48 of the post-test documentation folders prior to completion of our fieldwork. Although affecting the scope of our originally planned audit work, we do not believe that these limitations affected the overall accomplishment of our audit objective. One area that did have some impact on the accomplishment of our audit objective was the way the testing process, as well as the test cases, changed as

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<sup>1</sup> The nine accounting functional areas included 1) Audit Trail, Security, and Internal Control; 2) Cost Accounting; 3) Fixed Assets; 4) M-Year Legislation; 5) Receipt and Acceptance; 6) Reimbursable Work Authorizations; 7) Reporting; 8) Taxable Transactions; and 9) Travel Advances and Obligations.

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we attempted to perform our audit analyses. Consequently, we were unable to reach a final conclusion on the nine accounting functional areas and, therefore, the IFS as a whole. However, our audit work did identify areas where we believe a degree of risk exists that the IFS may not meet the Joint Financial Management Improvement Program's (JFMIP)<sup>2</sup> requirements or where requirements will only be met through workarounds.

- E. Discussed with subject matter experts the extent of the security audit trail detail (such as employee login and activity while on the system) and how it will function after implementation of the IFS.
  - F. Discussed with subject matter experts if auditability functions are being contemplated for the IFS.
- II. Verified data conversion plans from the legacy financial system to the IFS were developed and testing was progressing.
- III. Followed-up on previously reported conditions contained in our requirements definition report<sup>3</sup> concerning 64 JFMIP requirements that were either missing or that were not fully addressed in the Systems Requirements Report.
- IV. Assessed the impact on compliance with laws and regulations of deleted or deferred requirements that were asserted to be functional by the software subcontractor, and the overall cost to the project.

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<sup>2</sup> The JFMIP is a joint undertaking of the United States Department of the Treasury, the Government Accountability Office (formerly the General Accounting Office), the Office of Management and Budget, and the Office of Personnel Management, working in cooperation with each other and other agencies to improve financial management practices in the Federal Government.

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**Appendix II**

**Major Contributors to This Report**

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Peter L. Stoughton, Auditor

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Some Accounting Standards or Contain Certain Functionality  
as Originally Asserted by the Vendor**

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**Appendix III**

**Report Distribution List**

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Appendix IV

Management's Response to the Draft Report



CHIEF FINANCIAL OFFICER

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

RECEIVED  
SEP 14 2004

September 14, 2004

MEMORANDUM FOR GORDON C. MILBOURN III  
ACTING DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:

*Eileen T. Powell*  
for Eileen T. Powell  
Chief Financial Officer

SUBJECT:

Draft Audit Report # 2004-10-003, "The Integrated  
Financial System Software Does Not Comply With Some  
Accounting Standards or Contain Certain Functionality As  
Originally Asserted by the Vendor"

Thank you for the opportunity to review and comment on your draft report, "The Integrated Financial System Software Does Not Comply With Some Accounting Standards or Contain Certain Functionality As Originally Asserted by the Vendor."

I agree with your recommendations. The IRS' objective for the Integrated Financial System (IFS) is to improve the IRS' ability to meet internal and external requirements with regard to management controls, performance measures, and reporting, as well as improve the quality and timeliness of cost and administrative activity data for IRS executives and managers.

I have attached a detailed response to each recommendation along with management corrective actions, proposed implementation dates, and responsible officials, as applicable.

Please extend my sincere appreciation to your audit staff. They provided excellent advice, conducted themselves in a professional manner, and worked extended hours and weekends to observe the execution of some key IFS test cases.

If you have any questions, please contact me at 202.622.6400, or have a member of your staff contact Susan Spurling-Marcus at 301.731.3555.

Attachment

**The Integrated Financial System Software Does Not Comply With  
Some Accounting Standards or Contain Certain Functionality  
as Originally Asserted by the Vendor**

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Attachment

THE INTEGRATED FINANCIAL SYSTEM SOFTWARE DOES NOT COMPLY WITH  
SOME ACCOUNTING STANDARDS OR CONTAIN CERTAIN  
FUNCTIONALITY AS ORIGINALLY ASSERTED BY THE VENDOR

RECOMMENDATION 1

The CFO should ensure all JFMIP and FFMIA requirements and accounting standards are operating before the IFS deployment. If this is not feasible, the IRS should move to the government version of the IFS as soon as possible, and the CFO should ensure these requirements are included in that version.

Corrective Action

Given the time scheduled for implementation and the complexity of the project, the CFO did everything possible to ensure relevant JFMIP and FFMIA requirements and accounting standards were delivered in Release 1 of IFS. The CFO will ensure those requirements not satisfied in Release 1 are implemented in subsequent enhancements or upgrades. However, as indicated in your report, subsequent planned releases of IFS have been put on hold due to the current IRS funding situation. Upon successful implementation of IFS, Release 1, the CFO will develop an action plan to address enhancements and future releases of IFS – especially the upgrade to the federalized version of SAP which should close many of the existing JFMIP gaps.

Planned Implementation Date

April 1, 2006

Responsible Official

Associate Chief Financial Officer for Internal Financial Management

RECOMMENDATION 2

The CFO, in concert with the Director of Procurement and the Associate CIO, Business Systems Modernization, should ensure a coordinated and united stance is taken when conducting any negotiations with the IFS contractor concerning the cost associated with the functionality of accounting requirements that were asserted to be ready for deployment by the software subcontractor.

Corrective Action

I have implemented your recommendation to coordinate the IFS contract negotiations with the Director, Procurement, and the Associate CIO, Business Systems Modernization.

Implementation Date

July 15, 2004



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Responsible Official

Associate Chief Financial Officer for Internal Financial Management

RECOMMENDATION 3

The CFO, in concert with the Director of Procurement and the Associate CIO, Business Systems Modernization, should ensure all costs are considered when any negotiations are held concerning system requirement deferrals.

Corrective Action

As recommended, we have worked together to ensure all costs associated with requirements that were asserted to be ready for deployment, by the software subcontractor, but not delivered in Release 1, were included in the negotiations. IRS' current contract is a cost-sharing contract where the IRS is responsible for 24% of the costs and the contractor is absorbing 76% of the costs incurred from May 1, 2004, through January 31, 2005.

Implementation Date

July 15, 2004

Responsible Official

Associate Chief Financial Officer for Internal Financial Management

RECOMMENDATION 4

The CFO should ensure the remaining JFMIP requirements are added to subsequent versions of the SRR and are included in future IFS releases.

Corrective Action

The CFO will ensure any requirements not satisfied in Release 1 are identified and implemented in subsequent enhancements or upgrades. However, as indicated in your report, subsequent planned releases of IFS have been put on hold due to the current IRS funding situation. Upon successful implementation of IFS, Release 1, the CFO will develop an action plan to address enhancements and future releases of IFS -- especially the upgrade to the federalized version of SAP which should close many of the existing JFMIP gaps.

Planned Implementation Date

April 1, 2006

Responsible Official

Associate Chief Financial Officer for Internal Financial Management

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Corrective Action Monitoring Plan

The CFO will continue to monitor all future IFS project proposals to ensure that JFMIP and FFMIA requirements and accounting standards that were not provided in the current release are identified and included in any future IFS upgrades or releases.