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TO: James M. Martin, Acting Deputy Chief Financial Officer, Office of the Chief Financial Officer, F

FROM:

Hanh T. Do, Director, Information Systems Audit Division, Office of Audit, GAA

SUBJECT: HUD Compliance With Joint Financial Management Improvement Program
Core Financial System Requirements for Cost Management

HIGHLIGHTS

What We Audited and Why

We audited certain components of the U.S. Department of Housing and Urban Development's (HUD) financial system to determine whether the financial system is capable of performing the cost management function as defined in Joint Financial Management Improvement Program (JFMIP)¹ publication number JFMIP-SR-02-01, "Core Financial System Requirements," dated November 2001.

We performed this audit because conformance with federal financial system requirements is one of several factors to be considered in our assessments of HUD compliance with Office of Management and Budget Circular A-127, "Financial Management Systems," and the Federal Financial Management Improvement Act.² Office of Management and Budget Circular A-127 incorporates JFMIP requirements.

¹ JFMIP is a joint undertaking of the U.S. Department of the Treasury, the General Accountability Office, the Office of Management and Budget, and the Office of Personnel Management to improve financial management practices and establish functional requirements for federal financial systems.

² The Federal Financial Management Improvement Act of 1996 requires auditors to report on agency compliance with federal financial management system requirements, federal accounting standards, and the U.S. Standard General Ledger as part of financial statement audit reports.

What We Found

HUD's core financial systems do not have the ability to perform all of the mandatory cost management functions specified in JFMIP's "Core Financial System Requirements" (JFMIP SR-02-01, November 2001). HUD's core financial systems lack the ability to accumulate nonfinancial data that would be needed to internally calculate cost management information. JFMIP mandatory requirement number CMA-06 requires that "the core financial system must provide the capability to accumulate non-financial data relating to cost objects such as output units to allow the calculation of both total and unit costs." Without this capability, HUD's core financial system does not provide all of the nonfinancial data elements needed to support the integration of budget, cost, and performance measures.

To obtain all of the cost information it needs for the integration of budget, cost, and performance measures, HUD depends on other sources of information. These sources include both automated and manual processes, procedures, controls, data, software, and support personnel that are not integrated through a common database or electronically interfaced with the core financial system.

What We Recommend

The Office of the Chief Financial Officer should develop compliant cost management functional requirements that support the integration of budget, cost, and performance measures as part of the HUD Integrated Financial Management Improvement Project.

Auditee's Response

HUD disagrees with our recommendation. However, we recently received the HUD Integrated Financial Management Improvement Project's "Detail-Level Functional Requirements Document" that includes a mandatory functional requirement for the accumulation of nonfinancial data. Based on this information, we are recording a management decision for this recommendation in the Department's Audits Management System with a target completion date of October 14, 2005. The complete text of the auditee's response, along with our evaluation of that response, can be found in appendix B of this report.

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BACKGROUND AND OBJECTIVES

The Joint Financial Management Improvement Program is a joint undertaking of the U.S. Department of the Treasury, the Government Accountability Office, the Office of Management and Budget's Office of Federal Financial Management, and the Office of Personnel Management. The heads of these agencies, also referred to as JFMIP principals,³ work in cooperation to improve financial management practices in the federal government.

Office of Management and Budget Circular A-127, "Financial Management Systems," incorporates JFMIP functional requirements in its financial management system requirements. JFMIP publication number JFMIP-SR-02-01, "Core Financial System Requirements," dated November 2001, provides functional requirements for federal financial systems. The requirements include functional requirements for cost management. According to the publication,

The Cost Management function of the Core Financial system attempts to measure the total cost and revenue of Federal programs, and their various elements, activities and outputs. Cost Management is essential for providing accurate program measurement information, performance measures, and financial statements with verifiable reporting of the cost of activities.

The publication specifies four processes for the cost management function:

- (1) Cost setup and accumulation (CMA) – process for identifying and tracking cost data for cost objectives.
- (2) Cost recognition (CMB) – process for determining when the results of an event are to be included in financial statements (e.g., use of accrual accounting).
- (3) Cost distribution (CMC) – process for distributing costs in accordance with Statement of Federal Financial Accounting Standard 4, "Managerial Cost Accounting Concepts and Standards for the Federal Government."
- (4) Working capital and revolving fund (CMD) – process for tracking service level agreements, verifying funds availability, billing customers, and measuring costs.

The publication provides

Once management has identified the cost objects it needs and the corresponding structure has been set up in the accounting system, the system accumulates cost data accordingly. Finally, cost information is prepared and

³ In December 2004, the JFMIP principals signed an agreement to realign responsibilities for financial management policy and oversight and JFMIP ceased to exist as a stand alone organization. The agreement reassigns responsibility for certifying financial system software from the Joint Financial Management Improvement Program to the Chief Financial Officers Council. The Office of Federal Financial Management will now issue requirements for financial systems.

distributed to managers. A “cost object” is any activity, output, outcome, or item whose cost and revenue are to be measured, such as, organizational units, programs, projects, targeted outputs, specific contracts, specific customers, work orders, and GPRA (Government Performance and Results Act) program/activities, etc.

HUD is responsible for establishing within its core financial system a cost management function that conforms with JFMIP requirements. The HUD Centralized Accounting Program System and the Project Cost Accounting System⁴ are HUD’s primary systems for carrying out this responsibility.

The HUD Centralized Accounting Program System is an implemented version of American Management System’s core financial system product, Federal Financial System version 5.6.2. Federal Financial System version 5.6 was certified as compliant through June 30, 2003.—While the JFMIP certification test comprehensively checks for compliance with required functionality, it does not address a number of factors related to an individual agency’s specific requirements, the operating environment (e.g., legacy systems such as Program Accounting System), performance in the agency’s environment, and ultimately, agency compliance with requirements. This should be evaluated prior to implementation.

The objective of our audit was to determine whether HUD’s core financial system, specifically the HUD Centralized Accounting Program System and Project Cost Accounting System, is capable of performing the cost management function as defined in JFMIP’s “Core Financial System Requirements.”

⁴ HUD uses the Project Cost Accounting System, which is an integrated Federal Financial System module to establish projects, specific contracts, and task orders as cost objects for HUD’s information technology projects in the Working Capital Fund.

RESULTS OF AUDIT

Finding 1: HUD's Core Financial System Does Not Meet the JFMIP Core Financial System Requirement for Ability to Accumulate Certain Types of Data for Use in Cost Management

We found that HUD's core financial systems do not have the ability to perform one of the mandatory cost management functions specified in JFMIP's "Core Financial System Requirements." HUD's core financial systems lack the ability to accumulate nonfinancial data that would be needed to internally calculate cost management information. JFMIP mandatory requirement number CMA-06 requires that "the core financial system must provide the capability to accumulate non-financial data relating to cost objects such as output units to allow the calculation of both total and unit costs." Without this capability, HUD's core financial system cannot provide the nonfinancial data elements to support the definition and use of cost objects⁵ by management and the integration of budget, cost, and performance measures, requiring HUD to obtain the information from sources outside the core financial system.

Cost management is essential for providing accurate program measurement information, performance measures, and financial statements with a verifiable report of the cost of activities. The cost setup and accumulation process of the cost management function identifies and tracks cost data associated with the specific cost objects required by management. It provides the data needed for accountability over the financial execution of public programs; meaningful comparisons to measure compliance with management policies; evaluation of the efficiency and economy of resources used in the various activities; and support for fees, services, or products. It also provides a basis for linking operational results (cost) to the budget and performance measures.

HUD's core financial system is not capable of accessing the nonfinancial data elements so that managerial cost information can be tailored to be useful to decision makers. This lack of capability indicates that HUD's core financial systems do not support the integration of budget, cost, and performance measurement data.

To obtain cost and budget information not accumulated and processed by the core financial system, HUD has developed other systems and processes to provide cost and performance measurement information as components of its integrated

⁵ A cost object is defined by JFMIP as "any activity, output, or item whose cost and revenue are to be measured, such as organizational units, programs, projects, targeted outputs, specific contracts, specific customers, work orders, and GPRA [Government Performance and Results Act] program/activities, etc."

financial management system to meet its internal and external reporting requirements. HUD has developed a financial data mart, which serves as the financial information data warehouse which HUD states has the capability to provide HUD management with much of the cost management information it needs. Other examples include, HUD's Total Estimation and Allocation Mechanism/ Resource Estimation and Allocation Process⁶ is described as the primary tool for estimating, justifying, and allocating its staffing resources used in budget formulation and execution, strategic planning, and organizational and management analyses. Also, the Office of Public and Indian Housing uses its information systems and other manual processes to accumulate the nonfinancial data associated with the \$18 billion worth of disbursements processed within its program areas. Additionally, HUD yearly performs a cost allocation study for use in the preparation of the year-end statement of net cost⁷ and uses the same allocation percentages—which may not reflect actual activity—in the preparation of the following year's quarterly financial statements.

The Director of HUD's Financial Systems Maintenance Division agreed that the HUD Central Accounting Program System does not contain nonfinancial data. He stated that the data are captured in HUD's programmatic and other business systems and that the Total Estimation and Allocation Mechanism/ Resource Estimation and Allocation Process consolidates that information for use in its performance reports. HUD's objective in developing this application was to develop time and workload data necessary for viable budget estimation and execution, strategic planning, organizational and management analyses, and to meet HUD's Government Performance and Results Act requirements.

HUD has an ongoing effort—HUD Integrated Financial Management Improvement Project—underway that is expected to result in an implemented integrated core financial system to include cost management requirements. If HUD develops strong requirements, the project will provide the cost and nonfinancial data needed for financial management and accountability over the financial execution of programs, meaningful comparisons to measure compliance with management policies, evaluation of the efficiency and economy of resources used in the various activities, and support for services. It should also provide a basis for linking operational results to the budget and performance measures.

⁶ Known within HUD as TEAM/REAP

⁷ Statement of Federal Financial Accounting Standards Number 4, "Managerial Cost Accounting Concepts and Standards for the Federal Governments," states that as long as the entity complies with the managerial cost accounting standards, it may use a cost accounting system or use cost finding techniques and other cost studies and analyses.

Conclusion

HUD's core financial system is not able to accumulate certain types of required management information necessary for the integration of detailed budget, financial, and programmatic data for use by HUD management.

Recommendations

We recommend that the Chief Financial Officer:

1. Develop Office of Federal Financial Management⁸ compliant cost management functional requirements that support the integration of budget, cost, and performance measures as part of the HUD Integrated Financial Management Improvement Project.

⁸ The Office of Federal Financial Management is the successor organization to the Joint Financial Management Improvement Program and is responsible for issuing federal financial management requirements.

SCOPE AND METHODOLOGY

This audit examined conformance of HUD's core financial systems with mandatory functional requirements for the cost management function provided in JFMIP "Core Financial System Requirements.

Our audit focused on whether HUD's core financial system, specifically the HUD Centralized Accounting Program System and Project Cost Accounting System, is capable of performing the cost management function as defined in "Core Financial System Requirements." We conducted interviews, reviewed documentation, and observed system operations and reports.

We performed audit work from April 2004 through April 2005. Our audit covered the period April 2004 through December 2004.

We performed our review in accordance with generally accepted government auditing standards.

INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

This review was an assessment of compliance with high-level functional requirements. We did not test or evaluate internal controls.

APPENDIX

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

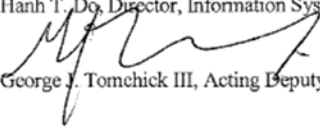


U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-3000

OFFICE OF THE CHIEF FINANCIAL OFFICER

SEP -9 2005

MEMORANDUM FOR: Hanh T. Do, Director, Information Systems Audits Division, GAA

FROM: 
George J. Tomchick III, Acting Deputy Chief Financial Officer, F

SUBJECT: Response to Draft Audit Report on HUD Compliance with Joint Financial Management Improvement Program Core Financial System Requirements for Cost Management

The Office of the Chief Financial Officer disagrees with the findings and recommendation in the subject draft report dated August 8, 2005. The draft report incorrectly draws the following conclusion:

HUD's core financial systems lack the ability to accumulate non-financial data that would be needed to internally calculate cost management information. JFMIP mandatory requirement number CMA-06 requires that "the core financial system must provide the capability to accumulate non-financial data relating to cost objects such as output units to allow the calculation of both total and unit costs."

As expressed in several previous meetings with your staff, HUD's Central Accounting and Program System (HUDCAPS) and the core Federal Financial System (FFS) software has cost management capability that is evidenced by:

- 1) Project cost accounting/cost allocation modules that are currently used to collect direct project costs and collect and distribute overhead (payroll) for the working capital fund projects. In the past, these modules were configured and used for a short period to collect and distribute costs for OIG's own Operation Safe Home Project.
- 2) Cost accumulation objects (non-financial) that the software supports and that HUD currently uses include: program, program activity, budget object, organization, project, contract, job and reporting category.

In addition, HUDCAPS and the core FFS software has cost management capability that HUD has not found cost beneficial to activate in the area of receipt of commodities. The system can be configured to require a receiver document (RC) to record quantity received and quantity accepted.

Comment 1

Comment 2

Comment 3

Comment 4

Comment 5

We also disagree with OIG's position that HUD's use of the financial data mart is not an acceptable means of providing cost management reporting for the department's managers and executives. HUD replaced the FFS COTS delivered Decision Support System (DSS) with the financial data mart in order to use more robust third party reporting tools that have allowed us to do better reporting at lower cost. The financial data mart made it possible to build joins between the general journal and subsidiary data bases that also improved cost management reporting. A reporting database was always part of the core COTS product and always part of HUDCAPS.

Going forward, OMB is setting the standards for Centers of Excellence (COE) for Financial Management and HUD must select a COE that meets OMB standards for implementation of the HUD Integrated Financial Management Improvement Project. The COE will be operating a certified core financial system for HUD. Therefore, OIG's proposed draft recommendation is unnecessary and not relevant in the current federal financial systems development environment.

Comment 6

I request that the conclusions and recommendation reflected in this draft report be reconsidered and revised or eliminated based on the facts of the matter. Should you or your staff have any questions on this response, please contact Gail Disc, Senior Advisor for Financial Systems Project Management, on 202-708-0614 extension 3749.

cc:

James Martin, Assistant CFO for Financial Management, FM
Gail Disc, Senior Advisor for Financial Systems Project Management, FY
Mary S. Matiella, Assistant Secretary for Accounting, FB
Larry McGhee, Director Audit Liaison Division, FMA
Tom Lear, Audit Liaison Division, FMA

OIG Evaluation of Auditee Comments

- Comment 1** The Office of the Chief Financial Officer is incorrect in stating that we found that HUD's core financial system does not have Cost Management capabilities. What we found is that HUD's core financial system does not have the capability to accumulate nonfinancial information, i.e. units. This mandatory requirement was one of eight cost accumulation and setup process functional requirements. In addition to the cost set up and accumulation process, there are three other cost management function processes. Our review of these other processes found no instance of noncompliance.
- Comment 2** This example is not relevant to a finding of noncompliance with the cost set up and accumulation process. The example illustrates capabilities found in the working capital and revolving fund process, which we reviewed and found compliant. Also, while OIG did develop functional requirements for Operation Safe Home, program funding was eliminated before the project cost system was implemented.
- Comment 3** This example is not relevant to a finding of noncompliance with the cost set up and accumulation process. The example illustrates capabilities found in the working capital and revolving fund process, which we reviewed and found compliant. We agree that the listed financial information classification elements are supported by HUD's core financial system. However our finding was that HUD's core financial system does not support the accumulation of nonfinancial information, i.e., units, within the core financial system.
- Comment 4** This example is not applicable because it refers to a required payment management function capability. Payment management was not evaluated in this review. While HUD should consider the cost-benefit of implementing a core financial system capability, HUD should ensure that it is in compliance with mandatory financial management requirements.
- Comment 5** We disagree with the Office of the Chief Financial Officer's statement regarding the datamart and financial reporting. HUD can use a datamart to provide an ad hoc financial reporting capability if the data that populates the datamart is derived from the core financial system. However, as indicated in the report, we found that nonfinancial data is not processed, accumulated, and summarized in the core financial system.
- Comment 6** We disagree with the observation that the recommendation is unnecessary. However, we recently received the HUD Integrated Financial Management Improvement Project's "Detail-Level Functional Requirements Document" dated August 9, 2005 that includes a mandatory functional requirement for the accumulation of nonfinancial data. Based on this information, we are recording a management decision for this recommendation in the Department's Audits Management System with a target completion date of October 14, 2005.