



Testimony

Before the Subcommittee on Federal Financial Management,
Government Information, Federal Services, and
International Security, Committee on Homeland Security
and Governmental Affairs, U.S. Senate

For Release on Delivery
Expected at 3:00 p.m. EDT
Thursday, June 28, 2007

HOMELAND SECURITY

Transforming Departmentwide Financial Management Systems Remains a Challenge

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Highlights of [GAO-07-1041T](#), a testimony before the Subcommittee on Federal Financial Management, Government Information, Federal Services, and International Security, Committee on Homeland Security and Governmental Affairs, U.S. Senate

Why GAO Did This Study

Since 2003, when the Department of Homeland Security (DHS) began operations, it has faced the difficult challenge of bringing together 22 diverse agencies and developing an integrated financial management system to provide reliable, timely, and useful financial information. GAO's 2007 report, *Homeland Security: Departmentwide Integrated Financial Management Systems Remain a Challenge*, GAO-07-536, emphasized the key issues related to DHS attempting to transform its financial management systems.

For today's hearing, this testimony, based on GAO's recent report, (1) summarizes DHS's financial system transformation efforts, (2) points out key financial system transformation challenges at DHS, and (3) highlights the building blocks that DHS should consider to form the foundation for successful financial management system transformation efforts.

What GAO Recommends

Though there are no recommendations in this statement, in its related report ([GAO-07-536](#)), GAO made six recommendations focused on the need for DHS to define a departmentwide financial management strategy and embrace best practices, including human capital practices, to foster its systems integration effort. DHS concurred with GAO's recommendations.

www.gao.gov/cgi-bin/getrpt?GAO-07-1041T.

To view the full product, including the scope and methodology, click on the link above. For more information, contact McCoy Williams at (202) 512-9095 or Keith Rhodes at (202) 512-6412.

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Transforming Departmentwide Financial Management Systems Remains a Challenge

What GAO Found

DHS began implementation of the Electronically Managing Enterprise Resources for Government Effectiveness and Efficiency (eMerge²) program in January 2004 to integrate financial management systems across the entire department and to address the multitude of financial management weaknesses DHS inherited. In December 2005, the DHS Chief Financial Officer (CFO) decided not to exercise the next contract option with the systems integrator, and by September 2006, DHS's new CFO stated that eMerge² was officially "dead." DHS officials have stated that about \$52 million was spent on this project before it was halted but could not provide documentation to support this amount. DHS's decision to end the project before spending an estimated \$229 million was prudent; however, the agency has made little progress since that time and as a result has missed an invaluable opportunity to address existing financial management problems.

While DHS officials have recognized the need for an integrated financial management system, the department has not yet developed an overall transformation strategy that includes financial management policies and procedures, standard business processes, a human capital strategy, and effective internal controls. DHS officials have acknowledged that the *Internal Controls Over Financial Reporting Playbook* issued in March 2007 has a policy and process focus and does not comprise a strategy for financial systems modernization. DHS's recently developed high-level financial management systems strategy, the *Transformation and Systems Consolidation*, focuses on leveraging existing systems investments across DHS components and is still in the early stages of development. More detailed implementation strategies will be necessary to fully address financial management system integration efforts.

Consolidating financial management systems for an entity as large and diverse as DHS poses significant management challenges. DHS also has an opportunity to reap substantial benefits by reengineering business processes and standardizing those processes in terms of both productivity gains and staff portability across the various components. Based on industry best practices, GAO has identified four key building blocks that will be critical to DHS's ability to successfully complete its financial management transformation:

- developing a concept of operations,
- defining standard business processes,
- developing a migration and/or implementation strategy for DHS components, and
- defining and effectively implementing disciplined processes necessary to properly manage the specific projects.

Fully embracing these four building blocks and human capital best practices will be critical to the success of any future financial management plan or strategy that addresses implementing and/or migrating to an integrated departmentwide financial management system at DHS.

Mr. Chairman and Members of the Subcommittee:

It is a pleasure to be here today to participate in this hearing on the Department of Homeland Security's (DHS) ongoing efforts to effectively modernize its financial management systems. Modern financial management systems are a critical component to instituting strong financial management as called for by the Chief Financial Officers (CFO) Act of 1990,¹ the Federal Financial Management Improvement Act of 1996,² and other legislation. Hearings such as this one today can be very useful to foster meaningful financial management reform.

Over the years, we have reported on various agencies' financial management system implementation failures. As we testified³ in March 2006, agencies continue to struggle with developing and implementing integrated financial management systems that achieve expected functionality within cost and timeliness goals. Our recent report,⁴ which was prepared at the request of this subcommittee, discusses in detail some of the most significant problems and observations we identified with DHS's financial management system modernization efforts. Since 2003, GAO has designated implementing and transforming DHS as high risk⁵ because the agency has yet to implement a corrective action plan that includes a comprehensive transformation strategy, and because its management systems—especially related to financial, information, acquisition, and human capital management—are not yet integrated and wholly operational. Today, we would like to provide our perspectives on the importance of DHS following best practices in developing and implementing its financial management systems. Specifically, we would like to

¹Pub. L. No. 101-576, 104 Stat. 2838 (Nov. 15, 1990). The Department of Homeland Security Financial Accountability Act of 2004, Pub. L. No. 108-330 § 3, 118 Stat. 1275, 1276 (Oct. 16, 2004), added DHS to the list of CFO Act agencies.

²Pub. L. No. 104-208, div. A., § 101(f), title VIII, 110 Stat. 3009, 3009-389 (Sept. 30, 1996).

³GAO, *Financial Management Systems: DHS Has an Opportunity to Incorporate Best Practices in Modernization Efforts*, [GAO-06-553T](#) (Washington, D.C.: Mar. 29, 2006).

⁴GAO, *Homeland Security: Departmentwide Integrated Financial Management Systems Remain a Challenge*, [GAO-07-536](#) (Washington, D.C.: June 21, 2007).

⁵GAO, *High-Risk Series: An Update*, [GAO-07-310](#) (Washington, D.C.: January 2007).

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- summarize DHS's financial management systems transformation efforts,
 - point out key financial management system transformation challenges at DHS, and
 - highlight the building blocks that form the foundation for successful financial management system transformation efforts.

Our statement is based upon our recently issued report,⁶ as well as our previous reports and testimonies, which were performed in accordance with U.S. generally accepted government auditing standards.

Background

Since DHS began operations in March 2003, as mandated by the Homeland Security Act of 2002,⁷ it has faced the daunting task of bringing together 22 diverse agencies and developing an integrated financial management system. DHS inherited many financial management weaknesses and vulnerabilities from the 22 agencies. Auditors had identified 30 reportable conditions,⁸ 18 of which were considered material internal control weaknesses⁹ in the components prior to the transfer to DHS. In fiscal year 2003, the DHS financial statement auditors reported 14 reportable conditions, of which 7 were considered to be material weaknesses. While incremental progress has been made, the material internal control weaknesses and financial reporting problems continued in fiscal year

⁶[GAO-07-536](#).

⁷Pub. L. No. 107-296, 116 Stat. 2135 (Nov. 25, 2002).

⁸Under standards issued by the American Institute of Certified Public Accountants (AICPA), reportable conditions are matters coming to the auditors' attention relating to significant deficiencies in the design or operation of internal controls that, in the auditors' judgment, could adversely affect the department's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The AICPA recently revised its guidance for audits of financial statements beginning on or after December 15, 2006, to replace the term "reportable condition" with "significant deficiency."

⁹A material weakness was previously defined as a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. The new definition of a material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected. According to AICPA guidance, this change is effective for audits of financial statements beginning on or after December 15, 2006.

2006. In fiscal year 2006, while the total number of reportable conditions decreased to 12, the number of material weaknesses increased to 10. Some of the more recent material weaknesses identified by the auditors include problems with fund balance with treasury, budgetary accounting, and intergovernmental balances.

In early March 2007, DHS officials issued the *Internal Controls Over Financial Reporting (ICOFR) Playbook*, a high-level plan with a stated purpose of addressing the existing internal control weaknesses. DHS officials have reported that the *ICOFR Playbook* draws from internal control best practices to establish a management control program that measures performance and provides accountability for improvement. DHS officials expect the *ICOFR Playbook* to guide DHS for the next several years through fundamental financial management improvement across the spectrum of financial activities supporting the agency's mission.

eMerge² Project Was Unsuccessful

DHS began implementation of the Electronically Managing Enterprise Resources for Government Effectiveness and Efficiency (eMerge²) program in January 2004 to integrate financial management systems across the entire department and to address the department's financial management weaknesses. eMerge² was expected to establish the strategic direction for migration, modernization, and integration of DHS financial, accounting, procurement, personnel, asset management, and travel systems, processes, and policies. In February 2005, the DHS CFO conducted a review of the eMerge² effort. DHS chose not to exercise the next contract option, and DHS's contract with Bearing Point, Inc. (Bearing Point), the systems integrator, to acquire and implement eMerge² expired in December 2005.

In March 2006, DHS's Deputy CFO testified¹⁰ that eMerge² was taking a new direction in that the department was going to perform an assessment of existing financial management systems at the component level to determine whether internal resources could be leveraged. DHS officials also reported that they were going to review the Office of Management and Budget's (OMB) Financial Management Line of Business initiative to assess whether migration to a shared service provider was a feasible

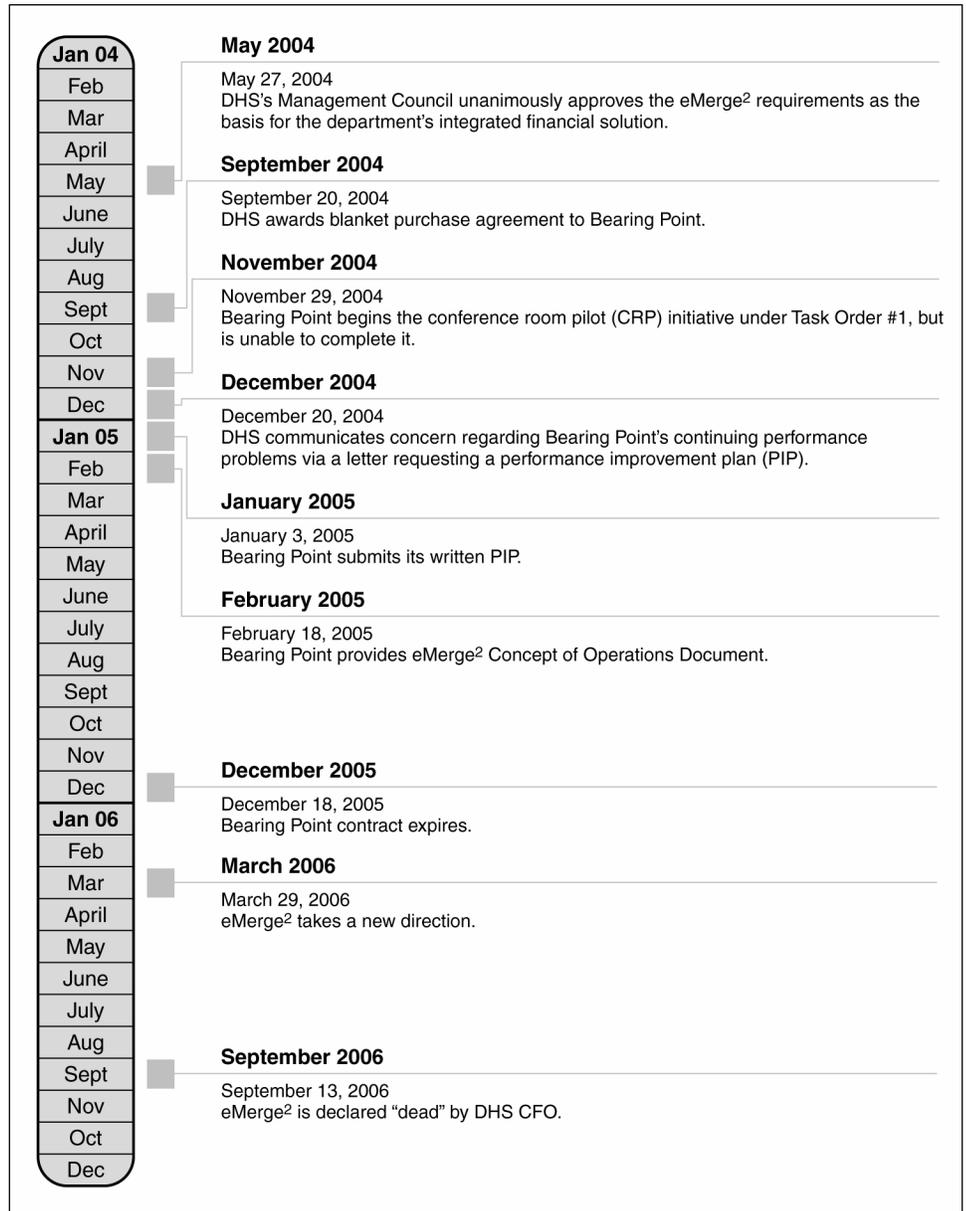
¹⁰Department of Homeland Security, March 29, 2006, testimony before the House Government Reform Subcommittee on Government Management, Finance, and Accountability and the House Homeland Security Subcommittee on Management, Integration, and Oversight.

option. In March 2006, we testified¹¹ that DHS was at an important crossroads in implementing a financial management system, and we discussed the necessary building blocks that form the foundation for successful financial management system implementation efforts.

Finally, in September 2006, the newly appointed CFO stated that eMerge² was officially “dead.” See figure 1 for a summary of the eMerge² timeline. DHS officials have stated that approximately \$52 million was spent on the eMerge² project before it was halted in December 2005. DHS could not provide any documentation to support these reported costs. DHS’s decision to end the project before spending an estimated \$229 million on a financial management system that would not provide the expected system functionality and desired performance was prudent, and we support the decision to cut its losses. However, the agency has made little progress since that time and has missed an invaluable opportunity to address existing financial management problems.

¹¹[GAO-06-553T](#).

Figure 1: Timeline of Key eMerge² Events



Source: GAO.

Financial Management Systems Transformation Efforts Are Incomplete

While DHS officials have recognized the need for an integrated financial management system, the department has not developed an overall financial management transformation strategy that includes financial management policies and procedures, standard business processes, a human capital strategy, and effective internal controls. DHS officials have acknowledged that the *ICOFR Playbook* has a policy and process focus and does not comprise a strategy for financial systems modernization. DHS's high-level financial management systems strategy, *Transformation and Systems Consolidation (TASC)*, focuses on leveraging existing systems investments across DHS components, and is still in the early stages of development. More detailed implementation strategies will be necessary to fully address financial management system integration efforts.

DHS recently provided us with its high-level strategy—TASC—which calls for DHS to consolidate its financial management systems into one of two models: the Transportation Security Administration (TSA) systems model or the U.S. Customs and Border Protection (CBP) systems model, which the department refers to as shared baselines. Some of the main objectives of this strategy are to realize cost savings and operational efficiencies, reduce the number of financial systems, and ensure that internal controls are embedded in these financial systems. DHS and OMB officials told us that OMB approved DHS's decision to rely on its in-house core financial management operations.

Our concern is that the components where the proposed shared baselines are currently in use have numerous financial management weaknesses and consequently do not appear to be good candidates to be the models for an entity with an annual budget in excess of \$40 billion. For example, the financial statement auditors for TSA reported¹² that TSA—which is serviced by the Coast Guard—was unable to provide sufficient evidential matter or make knowledgeable representations to support fiscal year 2005 and 2006 transactions and account balances, particularly for budgetary accounting and undelivered orders and property, plant, and equipment, among others. While DHS officials have stated that TSA's audit shortcomings were centered on policies and procedures and are not systems-oriented problems, our analysis of the auditor's report indicated that the problems were broad based. As DHS has recognized, success in

¹²Department of Homeland Security, *Performance and Accountability Report Fiscal Year 2006* (Washington, D.C.: November 2006).

financial management rests upon a comprehensive framework of people, policies, processes, systems, and assurance. Accordingly, it is imperative that DHS fully understands the policy and procedures weaknesses at TSA in order to prevent such weaknesses from affecting subsequent users.

In addition, the TASC strategy document and other draft documents DHS recently provided to us are incomplete. The documents provide a high-level perspective of the systems comprising the TSA shared baseline and broad time frames for migrating various DHS components. Much more detailed planning is needed to ensure that DHS has a solid foundation and road map for this transformation effort. For example, it is not clear which DHS component is expected to host¹³ the TSA shared baseline and what other services will be provided. Issues related to how this change will affect DHS's human capital are not yet addressed. Further, the TASC strategy does not address the CBP baseline nor, most importantly, how these various systems will ultimately be unified for departmentwide information needs. Much more detail is needed to provide a financial management strategy or plan for integrating and modernizing DHS's financial management systems.

Moreover, we would like to highlight the need for a close interrelationship between TASC and the *ICOFR Playbook*. The *ICOFR Playbook* calls for policies and procedures to be developed in a variety of financial management areas, such as intragovernmental transactions; legal and other liabilities; budgetary accounting; property, plant, and equipment; and operating materials and supplies. It is important that these policies and procedures be embedded in the financial systems that are discussed in TASC so that rework is minimized. While the *ICOFR Playbook* in particular continues to focus primarily on getting a "clean" audit opinion on DHS's annual financial statements, getting a "clean" audit opinion, although important, is not the end goal. The end goal is to establish a fully functioning CFO operation that includes (1) modern financial systems that provide reliable, timely, and useful information to support day-to-day decision making and oversight and for the systematic measurement of performance; (2) a cadre of highly qualified senior-level and supporting staff; and (3) sound internal controls that safeguard assets and ensure proper accountability. Ultimately, DHS must be able to provide reliable,

¹³Information technology hosting involves providing secure facility space, networks, and hardware to host software applications and providing the necessary personnel to operate this secure environment.

useful, and timely financial management information so that DHS leadership and the Congress are well positioned to make fully informed decisions to secure America's homeland.

Four Key Building Blocks and Effective Human Capital Management Must Drive DHS's Financial Management Transformation Efforts

Mr. Chairman, at this time I would like to point out that based on industry best practices, we have identified four key building blocks that will be critical to DHS's ability to successfully complete its financial transformation. Our March 2006 testimony¹⁴ and, more recently, our report for this subcommittee,¹⁵ pointed out that careful consideration of these four concepts, each one building upon the next, will be integral to the success of DHS's strategy. The four concepts are (1) developing a concept of operations, (2) defining standard business processes, (3) developing a migration and/or implementation strategy for DHS components, and (4) defining and effectively implementing disciplined processes necessary to properly manage the specific projects. Fully embracing these four building blocks and human capital best practices will be critical to the success of any future financial management system plan or strategy for transforming departmentwide financial management systems at DHS. We have continued to refine these key issues to ensure they remain closely aligned with DHS's stated approach—most recently, the department's TASC strategy.

DHS also has an opportunity to reap substantial benefits by reengineering business processes and standardizing those processes to realize productivity gains and staff portability across the various components. In addition, identifying staff with the requisite skills to implement such systems and identifying gaps in needed staff skills and filling them are necessary to successfully implementing and operating a new financial management system. Any DHS financial management system transformation plan or strategy will be inherently complex and challenging, making the adoption of best practices even more important for this undertaking. Table 1 highlights the key issues to be considered for each of the four areas.

¹⁴GAO-06-553T.

¹⁵GAO-07-536.

Table 1: Key Issues for DHS to Consider Based on the Four Building Blocks

Building block	Key issues
<i>Concept of operations:</i> Describe systems characteristics for a proposed system from a user’s perspective	<ul style="list-style-type: none"> • Define how DHS’s day-to-day financial management operations are and will be carried out to meet mission needs. • Clarify which component and departmentwide systems are considered financial management systems. • Include a transition strategy that is useful for developing an understanding of how and when changes will occur. • Develop an approach for obtaining reliable information on the costs of its financial management systems investments. • Link DHS’s concept of operations to its enterprise architecture.
<i>Standard business process:</i> Identify preferred business processes to standardize applications and training and portability of staff	<ul style="list-style-type: none"> • Assign responsibility for developing departmentwide standard business processes that meet the needs of its component agencies. • Develop an approach to encourage agencies to adopt new processes rather than selecting other methods that simply automate old ways of doing business. • Provide a foundation for component efforts to describe the business processes needed for unique missions, or develop subprocesses to support those at the departmentwide level.
<i>Strategy for implementing the shared baseline approach:</i> Utilize a detailed plan to consolidate financial management operations	<ul style="list-style-type: none"> • Develop specific criteria for requiring component agencies to migrate to one of the shared baselines rather than attempting to develop and implement their own stovepiped business systems. • Provide the necessary information for a component agency to make a selection of a shared baseline system. • Define and instill new values, norms, and behaviors within component agencies that support new ways of doing work and overcoming resistance to change. • Build consensus among customers and stakeholders on specific changes designed to better meet their needs. • Plan, test, and implement all aspects of the transition from one organizational structure and business process to another.
<i>Disciplined processes:</i> Reduce development time and enhance effectiveness by adopting industry standards and best practices	<ul style="list-style-type: none"> • Incorporate industry standards and best practices into DHS-wide guidance related to financial management systems implementation efforts. • Take actions to reduce risks and costs associated with data conversion and interface efforts. • Adopt an oversight process to ensure that modernization efforts effectively implement the prescribed policies and procedures.

Source: GAO.

As we previously stated, effective human capital management is critical to the success of any transformation effort. We reported in our *Executive Guide: Creating Value Through World-class Financial Management*¹⁶ that having staff with the appropriate skills is key to achieving financial

¹⁶ [GAO/AIMD-00-134](#).

management improvements, and managing an organization's employees is essential to achieving results. Strategic human capital management for financial management projects includes organizational planning, staff acquisition, and team development. The independent public accountants who conducted DHS's fiscal year 2006 audit have stated that many of the department's difficulties in financial management and reporting can be attributed to the original stand-up of a large, new, and complex executive branch agency without adequate organizational expertise in financial management and accounting. Moreover, DHS's Resource Management Transformation Office officials have stated that because of staffing shortages, outside contractors are currently performing some of the financial management activities or duties that internal DHS staff would normally perform. Some of the most pressing human capital challenges at DHS include (1) successfully completing its ongoing transformation; (2) forging a unified results-oriented culture across the department; (3) obtaining, developing, providing incentives to, and retaining needed talent; and (4) most importantly, maintaining leadership at the top, to include a chief operating officer or chief management officer.

Having adequate and sufficient human resources with the requisite training and experience to successfully implement a financial management system is a critical success factor. Strategic human capital planning is necessary for all stages of a financial systems implementation. Agencies across the federal government face the challenge of sustaining the momentum of transformation because of the limited tenure of key administration officials. Managing the transformation of financial management systems at an organization the size and complexity of DHS requires comprehensive coordinated planning and integration of key management functions across all components of the department.

In our related report, released today, we made six recommendations focused on the need for DHS to develop a financial management plan or strategy and to fully adopt the building blocks and human capital practices that are vital to minimizing the risk related to modernizing its financial management systems. In written comments on a draft of this report, DHS concurred with our recommendations and described the approach and steps that are planned to improve DHS's financial management systems.

Concluding Observations

GAO and others have found that the key to implementing systems that meet cost, schedule, and performance objectives is to have effectively implemented the disciplined processes necessary to reduce risks to acceptable levels. Ending eMerge² was a prudent decision; however, we

are concerned that DHS still lacks a clearly defined financial management strategy or financial management system implementation effort to even begin to address the integration and transformation issues highlighted in our most recent high-risk report.

Given that DHS is one of the largest and most complex executive branch agencies in the federal government, developing, operating, maintaining, and transforming its financial management systems represent a monumental challenge. This challenge is compounded by the relatively recent creation of DHS and the poor condition of the range of legacy financial and related business systems it inherited. Critical success factors for DHS's transformation efforts will include using the four building blocks and human capital best practices to provide reasonable assurance that the risks associated with implementing a departmentwide integrated financial management system are minimized. If properly implemented, the recommendations included in our related report released today, which are based on best practices, will help reduce the risk associated with a project of this magnitude and importance to an acceptable level. Otherwise, DHS runs the risk of repeating the failure of eMerge². At the request of this subcommittee, this testimony summarizes the results of our first review of DHS's financial management transformation efforts. We look forward to continuing to work with you as we continue to monitor DHS's efforts to transform its financial management systems. As DHS moves forward, your subcommittee's continuing efforts to oversee the status of this transformation will be critical to its success.

Mr. Chairman, this concludes our prepared statement. We will be happy to respond to any questions you or other members of the subcommittee may have at this time.

Contacts and Acknowledgments

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