

MEMORANDUM

To: Members of the Subcommittee on National Security, Emerging Threats and International Relations

Members of the Subcommittee on Technology, Information Policy, Intergovernmental Relations and Census

From: Vincent Chase, Chief Investigator

Date: March 26, 2003

Subject: Briefing memorandum for the hearing entitled, *Strengthening Oversight of DOD Business Systems Modernization*, scheduled for Monday, March 31st at 1:00 p.m., room 2154 Rayburn House Office Building.

PURPOSE OF HEARING

The purpose of the hearing is to examine and evaluate the effectiveness of DOD management and oversight of Defense Financial and Accounting Service (DFAS) information technology (IT) investments.

HEARING ISSUE

- 1. How does DOD ensure Defense Finance and Accounting Service (DFAS) information technology (IT) projects will be implemented within acceptable costs and reasonable timeframes?**
- 2. What is the Department of Defense information technology (IT) procurement strategy for DFAS?**

BACKGROUND

In 1991, the Department of Defense (DOD) established the Defense Finance and Accounting Service (DFAS) to standardize finance and accounting policies, procedures, and business systems. **(Web Resource 1)**

This action was taken to address problems encountered by the military services and agencies, problems caused by incompatible finance and accounting operations and the inherent inefficiency when multiple organizations perform virtually identical financial management and accounting functions.

Organizationally, DFAS is under the direction of the Under Secretary of Defense (Comptroller).

DFAS, as the DOD central accounting agency, is responsible for:

- recording and processing accounting transactions;
- paying vendors, contractors, and military and civilian employees;
- preparing reports used by DOD managers and by Congress; and,
- preparing DOD-wide and service specific financial statements required by the Chief Financial Officers Act.¹

DFAS fiscal year 2002 financial operations included:

<u>Type of activity</u>	<u>Volume of activity</u>
• Accounting transactions	124 million
• Disbursements made	\$346.6 billion
• Invoices paid	11.2 million
• Payroll and retirement payments	5.7 million
• Active DOD appropriations	267

Source: GAO Report-03-465

¹ 31 U.S.C. 3515

Federal spending on information technology doubled between 1997 and 2001. According to GAO, the Department of Defense remains the largest buyer of IT products and services to support the operation, maintenance, and modernization of DOD business systems. **(Attachment 1)**

DOD's fiscal year 2003 IT budget request was over \$26 billion. Of that amount, approximately \$18 billion will be used to support DOD business systems. The remaining \$8 billion funds the National Security System, which represents any telecommunications or information system operated by DOD which involves command and control of military forces and involves equipment that is an integral part of a weapon or weapon system.

The Defense Finance and Accounting Service fiscal year 2003 IT budgetary request was approximately \$494 million. Of that amount, \$353 million relates to the operation and maintenance of existing DFAS systems and the remaining \$141 million is for the modernization of systems.

(Web Resource 1)

According to GAO, DFAS has had limited success in improving the financial operations of the Department. DOD financial management problems are the result of challenges in the areas of human capital, processes (internal controls), and the Department's inability to modernize business systems effectively. **(Web Resource 2)**

During a Subcommittee oversight hearing on March 7, 2001, GAO testified unreliable cost and budget information negatively affects DOD ability to measure performance, reduce costs and maintain adequate fund control.

(Web Resource 3)

As a follow-up to that Subcommittee hearing, GAO was asked to study and evaluate DFAS' control and oversight of numerous financial management systems improvement initiatives. **(Attachment 2)** The study, *DOD BUSINESS SYSTEMS MODERNIZATION: Continued Investment in Key Accounting Systems Needs to be Justified*, is the subject of the March 31, 2003 hearing. **(Attachment 3)**

Business Systems Oversight

Within DOD's current organizational structure, the military services and agencies, for the most part, are responsible for managing and overseeing their respective information technology (IT) investments. The exceptions are those systems designed as major acquisition systems programs, which are under the auspices of DOD's Chief Information Officer (CIO).

More specifically, major acquisition systems are defined as IT projects with (1) program costs in any single year that exceed \$32 million, (2) total program costs that exceed \$126 million, or (3) total life cycle costs that exceed \$378 million. The life cycle cost is the total cost to the government for an information system over its expected useful life and includes the costs to acquire, operate, maintain, and dispose of the system.²

In addition, DOD policy³ requires major IT investments to be justified by an economic analysis. The policy states the economic analysis is to reflect both the life-cycle cost and benefit estimates, including a return-on-investment calculation, to demonstrate that the proposed investment is economically justified before it is made. **(Attachment 2, p.18)**

The Clinger-Cohen Act⁴ and the Office of Management and Budget (OMB) Circular A-130 require agencies to design and implement a process for assessing and managing the risks of information technology acquisitions to include analyzing, tracking, evaluating, and reporting on risks and results of all major information technology capital investments.

When acquiring major IT systems, the Clinger-Cohen Act requires the Chief Information Officer (CIO) to monitor and evaluate the performance of information technology programs and advise the heads of agencies whether to continue, modify, or terminate a program.

The Clinger-Cohen Act of 1996, OMB Circular A-130, DOD policy, and practices of leading organizations⁵ provide an effective framework for

² DOD Regulation 5000.2-R, Mandatory Procedures for Major Defense Acquisition Programs and Major Automated Information Systems Acquisition Programs, March 15, 1996 (revised June 2001).

³ Ibid.

⁴ 41USC Sec. 251 (The Clinger-Cohen Act of 1996).

managing information technology investments, not just when a program is initiated, but continuously throughout the life of the program.

DFAS Business Systems

At the Subcommittee's request, the General Accounting Office identified and reviewed four DFAS business system projects. DOD has invested approximately \$316 million in these projects. The projects reviewed were:

- DFAS Corporate Database/Corporate Warehouse (DCD/DCW)--The DCD is intended to interface, standardize, and share data between DOD financial systems. The purpose of the DCW is to provide central data warehouse capability to store, query, and report DOD financial data.
- Defense Procurement Payment System (DPPS)--DPPS is intended to be the standard, automated information system supporting the authorization of contract and vendor payments for DOD by consolidating eight legacy systems.
- Defense Standard Disbursing System (DSDS)-- DSDS is intended to standardize DOD's disbursement system to make payments and record disbursement transactions. DOD planned to eliminate four disbursing systems on deployment of DSDS.
- Defense Departmental Reporting System (DDRS)--DDRS is intended to standardize DOD's financial reporting process, produce standard DOD financial statements, and produce monthly budgetary reports based on the U.S. Standard Ledger by reducing the number of departmental reporting systems from seven to one

The President has made financial management and the use of technology integral to his fiscal year 2002 *Management Agenda* (**Web Resource 4**) for making the federal government more focused on results. In addition, in July 2001 the Secretary of Defense identified the modernization of DOD's financial management and business operations as one of his top priorities.

⁵ Statement of Joel C. Willemssen, Managing Director, Information Technology Issues, U.S. General Accounting Office, NSVAIR Subcommittee hearing record, p.5, *The Standard Procurement System (SPS): Can the DOD Procurement Process be Standardized?*, February 7, 2002.

In a letter to Vice-President Cheney, the Under Secretary of Defense Dov S. Zakheim stated, “The Department is taking aggressive action to correct financial management system deficiencies in order to improve financial management information. The Financial Management Modernization Program was established to implement the Secretary’s goal of providing timely, accurate, and reliable financial information.” **(Attachment 5)**

DISCUSSION OF HEARING ISSUE(S)

1. How does DOD ensure Defense Finance and Accounting Service (DFAS) information technology (IT) projects will be implemented within acceptable costs and reasonable timeframes?

Each year the Defense Finance and Accounting Service spends millions of dollars on financial management system initiatives to improve the accuracy of the agency’s financial and accounting functions. In July 2001, DOD announced that it would be seeking additional funding to improve financial management systems. Funding is part of the solution to improving DOD’s current system environment. However, a key ingredient to success is effectively managing and overseeing these investments. **(Attachment 4)**

Long-standing DOD financial management and business modernization problems result in a lack of information needed to make sound decisions, hinder the efficiency of operations and leave the Department of Defense vulnerable to waste. The DOD Comptroller and the DOD CIO are responsible for the evaluation and economic justification of new IT projects.

During previous hearings the Subcommittee found DOD has a poor record for controlling the proliferation of incompatible IT systems⁶, acquiring new systems that meet user needs within reasonable time frames,⁷ controlling acquisition and upgrade costs, and ensuring the quality of data. In addition, the General Accounting Office and the DOD Inspector General have

⁶ National Security, Veterans Affairs and International Relations Subcommittee Hearing, GPO Serial No 107-40, *Defense Security Service: Mission Degradation,*? March 2, 2001.

⁷ National Security, Veterans Affairs and International Relations Subcommittee Hearing, GPO Serial No 107-144, *The Standard Procurement System (SPS): Can The DOD Procurement Process Be Standardized,* February 7, 2002.

reported a variety of problems regarding DOD efforts to modernize IT business systems. **(Web Resource 6)**

According to GAO, the Department of Defense has not effectively managed and overseen the planned investment of over \$1 billion in four DFAS business system projects. Despite the investment of approximately \$316 million, and 4 to 7 years of development effort, there is no assurance the four DFAS business projects will improve accuracy and reliability of DOD financial management information.

According to General Accounting Office, DOD is not effectively overseeing DFAS IT investments. The DOD Comptroller, the DOD CIO and DFAS permitted each project to proceed despite the absence of the requisite economic analysis to demonstrate the projects would produce value commensurate with the cost being incurred. **(Attachment 3)**

- **DFAS Corporate Database/Corporate Warehouse (DCD/DCW)**

DCD is intended to facilitate the sharing of all DOD financial data among systems and functions, and applications and users. When deployed DCD/DCW will provide central data warehouse capability to store, query, and report DOD financial data. DCW is intended to serve as a shared data warehouse that provides uniform, centralized information to DOD's systems.

In May 2000, the Director of DFAS granted approval to continue development of the DCD/DCW with a condition that an economic analysis be completed in two months. In November 2000, four months after the economic analysis was due, it still had not been completed. The DFAS CIO verbally granted a waiver for development of the DCD economic analysis, which allowed the project to continue without a valid, well-supported justification. According to GAO, DCD project management officials stated that the analysis was not finalized because they were unable to agree on how to compute the return on investment and demonstrate that benefits exceeded costs.

The economic analysis consists of a life cost and benefit estimate, including a return on investment calculation that should be used by

decision-makers to determine whether the project investment is economically justified.

DCD/DCW project management is unable to compute the return on investment and demonstrate that benefits exceeded costs as a result of unsupported analysis documentation. Decision-makers were not provided with the basis for judging whether any of the proposed alternatives were worth the cost or whether the project was economically justified.

According to GAO, the DCD/DCW program manager acknowledged program requirements have yet to be fully defined. The program manager reported the draft Operational Requirements Document identified 102 change requests. These changes must be resolved before the document can be finalized. The projected completion date is May 2003. However, this completion date maybe optimistic. As a result of the changing requirements, the project manager estimated that DCD/DCW would not achieve full operational capability until fiscal year 2005, a four- year delay. In addition, the lack of defined user requirements caused an estimated total life cycle cost increase of approximately \$40 million from the original DCD/DCW life-cycle cost.

In a December 2000 report, the DOD IG raised concerns about the overall feasibility of DFAS being able to achieve the goal of a single, integrated system under the existing DCD systems development process. The report notes the risks are high because DOD management and oversight focus on individual systems rather than a comprehensive oversight of interdependent systems and processes.

In addition, DFAS owns only 48 of the 168 critical accounting, finance, and feeder systems that provide financial management data. Therefore, DOD cannot be sure DCD/DCW will succeed in creating a single integrated financial management system, standardize business processes, reduce the number of finance, accounting, and feeder systems, reduce costs or produce reliable, accurate and auditable financial information. According to GAO, the concerns raised by the DOD IG still remain today. **(Web Resource 6)**

- **Defense Procurement Payment System (DPPS)**

DPPS is intended to be the standard, automated information system supporting contract and vendor payments. According to GAO, key decision-making documents were never completed for DPPS. For instance, (1) a log documenting changes to the 1998 Acquisition Program Baseline was not maintained, and (2) DFAS officials were unable to provide GAO with a copy of the Acquisition Strategy. These documents are crucial for making and tracking strategic decisions and overseeing the project. Without a measurement of system alternatives, controls to track changes made to the system, cost growth, and expected performance, it is difficult to exercise effective management oversight.

DPPS is directly dependent on the DCD/DCW and the successful implementation of DOD-wide business rules for accounting, contracting, and finance to support the end-to-end procurement solution for contract and vendor payments.

Contract management has been a long-standing problem in DOD. However, GAO found DPPS lacks a fully defined end-to-end procurement and requirements solution. The lack of definition contributed significantly to a 5-year schedule delay and the estimated cost doubling, to \$552 million.

DOD plans to terminate DPPS after an investment of approximately \$270 million due to poor program performance and increasing costs.

- **Defense Standard Disbursing System (DSDS)**

DSDS is intended to standardize DOD's disbursement system to make payments and record disbursement transactions.

A change in DSDS system architecture and implementation strategy has resulted in a four-year delay in the completion of DSDS. According to GAO, user requirements are being continually modified. Since 1999, approximately 66 percent of these requirements have been changed.

At the time the requirements were established, DFAS acknowledged that key areas such as the deployment approach required additional analysis and definition. DOD's failure to define or complete system requirements resulted in DFAS inability to meet schedules or performance goals. In addition, the cost estimate for DSDS was not developed until September 2000. This estimate had not been updated since then even though DSD had experienced a 4-year schedule slippage.

- **Defense Departmental Reporting System (DDRS)**

DDRS is intended to standardize DOD's financial reporting process and produce standard DOD financial statements. The economic analysis to justify this initiative was developed in October 1998. The original cost estimate has grown from \$52 million to a current estimate of \$151 million. The program is five years behind schedule. According to GAO, the economic analysis has not been updated to reflect the known changes in project costs and schedule.

In addition, the intended system mission to prepare accurate and auditable financial and budgetary reports is in doubt. DDRS will not be able to produce auditable financial statements or have audit trail capability because the data from feeder systems, which are outside the control of DFAS and provide approximately 80 percent of the data the DOD needs for financial reporting purposes, are not reliable.

2. What is the Department of Defense information technology (IT) procurement strategy for DFAS?

The Department of Defense is investing billions of dollars annually in hundreds of systems that perform the same function spread across numerous DOD components. According to GAO, this proliferation of systems has

resulted because DOD's parochial operations have permitted each of the military services and agencies to manage and oversee their IT business system investments.

On September 10, 2001, Secretary of Defense Rumsfeld announced a broad initiative intended to transform the way the Department works, and what it works on, which he estimated could save 5 percent of DOD's budget, or an estimated \$15 to \$18 billion annually. The Secretary recognized that transformation would be difficult and expected the needed changes to take eight or more years to complete.

To achieve this ambitious goal, the Department established the Financial Management Modernization Program (FMMP) to implement the Secretary's goal of providing timely, accurate, and reliable financial information. The FMMP is creating an enterprise architecture that will serve as a plan of action linking IT systems and business processes in a comprehensive and integrated fashion. The functional areas for these systems and processes include accounting, finance, financial reporting, inventory, budget formulation acquisition, payroll, and cost management.

In August and October 2001, Dr. Dov Zakheim issued policy directives designated to constrain technology investments for new developmental and system modification initiatives during the design phase of the enterprise architecture. In developing and implementing the enterprise architecture, DOD needs to ensure DFAS business systems development are designed as an integral part of the architecture.

However, because investment management and oversight of key DFAS business systems has been ineffective, it is unclear how DOD intends to ensure current DFAS system development are designed as an integral part of the enterprise architecture.

In April 2002, DOD announced the Department had signed a contract with IBM to lead a team to develop the enterprise architecture. The IBM team will take more than 1,000 individual "feeder" IT systems and replace them with a more rational method of financial management.

According to the Under Secretary of Defense (Comptroller), "there is no way the present (financial management) system will lead to financial

statements that pass any kind of muster with auditors worth their salt.” The Comptroller indicated the current 1700 plus IT systems cannot operate in a coherent, interrelated fashion. Reducing the number of IT financial management systems by 90 percent would give DOD decision makers reliable, accurate and time financial management information.

(Attachment 6)

In addition, the enterprise architecture will also outline department-wide financial management standards and prescribe stringent internal controls before new systems are acquired. DOD expects to finish the architecture by March 2003 and then will begin testing the solution developed by the IBM team in early 2004.

However, some believe the timeframe to develop the new enterprise architecture is not realistic citing the Corporate Information Management (CIM) program as an example. In 1989 the Department of Defense began the CIM program with the intent of implementing standard systems across DOD. After 8 years and an investment of \$20 billion⁸ the effort was abandoned. According to GAO, CIM was abandoned due resistance between DOD components and a lack of sustained commitment to the program. Some military departments did not want to participate in CIM⁷ believing their financial management systems were superior to what was being proposed under CIM. Instead of centralizing responsibility for CIM, the services and defense agencies continued to operate in a business-as-usual manner, maintaining their service parochialism.

ATTACHMENTS

1. *Contracting for Information Technology Services*, GAO-03-384R, February 14, 2003.
2. Letter dated September 19, 2001 from Christopher Shays, Chairman-National Security, Veterans Affairs and International Relations

⁸ US General Accounting Office, High-Risk Series: Information Management and Technology, GAO/HR-97-9, February 1997.

Subcommittee to David M. Walker, Comptroller General of the United States.

3. General Accounting Office, *DOD BUSINESS SYSTEMS MODERNIZATION: Continued Investment in Key Accounting Systems Needs to be Justified*, GAO-03-465, February 2003.
4. *DOD's Battle To Balance Its Books*, Federal Computer Week, Christopher J. Dorobek, September 17, 2001.
5. Letter dated February 27, 2002 from Under Secretary of Defense Dov S. Zakheim to The Honorable Richard B. Cheney, President of the Senate, United States Senate.
6. Government Executive Magazine, *Defense Issues Contract to Fix Financial Systems*, Jim Garamore, American Forces Press Service, April 11, 2002.

WEB RESOURCES

1. The Defense Finance and Accounting Service
< <http://www.dfas.mil/agency/index.htm> >
2. General Accounting Office, *High-Risk Series: An Update*, GAO-03-119, January 2003.
< <http://www.gao.gov/> >
3. National Security, Veterans Affairs and International Relations Subcommittee Hearing, GPO Serial No 107-22, *Vulnerabilities to Waste, Fraud, and Abuse: General Accounting Office Views on National Defense and International Relations*, pg. 15, March 7, 2001.
< <http://www.gpo.gov/congress/house/house07ch107.html> >
4. *President's Management Agenda-Fiscal Year 2002*
< http://www.whitehouse.gov/omb/budintegration/pma_index.html >
5. National Security, Veterans Affairs and International Relations Subcommittee Hearing, GPO Serial No 107-144, *The Standard Procurement System (SPS): Can The DOD Procurement Process Be Standardized*, February 7, 2002.

< <http://www.gpo.gov/congress/house/house07ch107.html>>

6. Department of Defense, Office of Inspector General, *Oversight of Defense Finance and Accounting Service Corporate Database Development*, December 28, 2000.

<<http://www.dodig.osd.mil/audit/reports/fy01/01-030.pdf>>

WITNESSES

Panel One

Mr. Randolph Hite, Director
Information Technology Architecture and Systems Issues
General Accounting Office

Mr. Gregory Kutz, Director
Financial Management and Assurance
General Accounting Office

Mr. Darby Smith, Assistant Director
Financial Management and Assurance
General Accounting Office

Panel Two

Ms. JoAnn Boutelle
Deputy Chief Financial Officer
Department of Defense

Mr. John R. Landon
Principal Director,
Deputy Assistant Secretary of Defense,
Command, Control, Communications, Intelligence, Surveillance,
Reconnaissance, Space & IT Programs

Mr. Thomas Bloom, Director
Defense Finance and Accounting Service (DFAS)
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