



**Office of the Chief Procurement Officer
Washington, DC**

HUD's Integrated Core Financial System



Issue Date: December 4, 2012

Audit Report Number: 2013-DP-0002

TO: Jemine A. Bryon, Chief Procurement Officer, N

FROM: //signed// Hanh T. Do, Director, Information Systems Audit Division, GAA

SUBJECT: Audit of Incorrect Payments to the Project Contractor for Data Conversion Tasks Related to the Implementation of HUD's Integrated Core Financial System

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of Incorrect Payments to the Project Contractor for Data Conversion Tasks Related to the Implementation of HUD's Integrated Core Financial System.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, section 8L, requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at <http://www.hudoig.gov>.

If you have any questions or comments about this report, please do not hesitate to call me at 202-402-8147 or Dorothy Bagley at 202-402-8139.



December 4, 2012

Audit of Incorrect Payments to the Project Contractor for Data Conversion Tasks Related to the Implementation of HUD's Integrated Core Financial System

Highlights

Audit Report 2013-DP-0002

What We Audited and Why

We audited the U.S. Department of Housing and Urban Development's (HUD)'s plans and procedures for data conversion of the HUD Integrated Core Financial System (ICFS). Our audit objective was to review HUD's readiness to fully implement ICFS and determine whether HUD had properly managed the payments related to data conversion activities.

We conducted this audit as a component of the testing of general and technical controls for information systems in connection with the annual audit of HUD's consolidated financial statements.

What We Recommend

We recommend that the Office of the Chief Procurement Officer (OCPO) obtain reimbursement for payment from the Project contractor for the incomplete contract tasks. Also, it should ensure that future fixed-price contracts require that a contract deliverable be associated with each payment on the partial payment schedule. Lastly, it should ensure that future fixed-price contracts with partial payment schedules include a requirement to withhold a percentage of the contracted amount for each task until the task is completed.

What We Found

OCFO incorrectly paid the Integrated Financial Management Improvement Project contractor for tasks that were not completed. Specifically, OCFO incorrectly paid more than \$1.3 million to the Project contractor for one contract task, although it did not receive the contract deliverables associated with those tasks. Also, OCFO paid the entire amount of another contract task before ensuring that the task had been completed.

TABLE OF CONTENTS

Background and Objectives	3
Results of Audit	
Finding 1: OCFO Did Not Ensure That Payments to the Project Contractor Were Correct	4
Scope and Methodology	8
Internal Controls	9
Appendixes	
A. Auditee Comments and OIG's Evaluation	10

BACKGROUND AND OBJECTIVES

The U.S. Department of Housing and Urban Development's (HUD)'s Integrated Financial Management Improvement Project, a project under the HUD Transformation Initiative, was created to facilitate the implementation of a new departmental core financial system, HUD's Integrated Core Financial System (ICFS). HUD plans for ICFS to replace the HUD Central Accounting and Program System (HUDCAPS)¹ and the Program Accounting System (PAS),² two of HUD's five³ main financial management applications.

The initial scheduled implementation date for ICFS was March 2012. In the summer of 2011, the Project contractor proposed changing the implementation date to May 2012. This new date was not formally approved. In March 2012, the project was stopped, and HUD began reevaluating its options for the Project. HUD could revise the Project plan to implement a "go live" in the first or second quarter of fiscal year 2013 or develop and implement a "phased" approach in fiscal year 2013 or 2014. This change in direction would require that HUD quickly address the risks; apply additional resources; and analyze contract, funding, and Project schedule issues. If this was not possible, another option was to cancel the implementation of ICFS and stay with HUDCAPS. However, staying with HUDCAPS would require enhancements to the legacy financial system over time to reduce risk associated with audit, security, financial reporting, and operational effectiveness. HUD is reassessing its options for the Project. To date, HUD has spent more than \$35 million on the Project.

Our audit objective was to review HUD's readiness to fully implement ICFS. Specifically, we wanted to determine whether HUD had properly managed the payments related to data conversion activities for the implementation of ICFS.

¹ HUDCAPS captures, reports, controls, and summarizes the results of the accounting processes, including budget execution and funds control, accounts receivable and collections, accounts payable, and the general ledger.

² PAS is an integrated subsidiary ledger for HUD's grant, subsidy, and loan programs. PAS maintains accounting records based on the receipt of funding authorizations from HUDCAPS, which generates transaction activity at different levels.

³ HUDCAPS, PAS, Hyperion - HUD's consolidated financial statement system, Financial DataMart, and the Line of Credit Control System

RESULTS OF AUDIT

Finding 1: OCFO Did Not Ensure That Payments to the Project Contractor Were Correct

The Office of the Chief Financial Officer (OCFO) incorrectly paid the Project contractor for data conversion tasks that were not completed. Specifically, OCFO paid (1) more than \$1.3 million to the Project contractor, although it did not receive the contract deliverables related to cutover tasks required for the implementation of ICFS and (2) for a contract task to build and unit test before ensuring that the task was completed. These conditions occurred because the payment schedule in the Project contract was not set up properly to comply with HUD regulations and meet the contract requirement. Also, a project deliverable review and approval process was not adequate. As a result, the Project contractor received a \$1.67 million payment for incomplete work and should have been paid only \$312,500. Also, OCFO could not ensure that the Project objectives were met.

OCFO Incorrectly Paid the Project Contractor for Tasks That Were Not Completed

OCFO incorrectly paid more than \$1.3 million to the Project contractor for the cutover⁴ contract task, although it did not receive the contract deliverables. In May 2012, a stop work order was issued, resulting in the reassessment of each contract task. Prior to the stop work order the Project contractor had received partial payments for cut over tasks totaling \$1.67 million.

As of June 4, 2012, the contractor had submitted only one of the seven contract deliverables. The Project contractor did not submit the contract deliverables that were due to HUD between December 2011 and March 2012. However, OCFO officials continued to make partial payments to the contractor.

Based on work that was completed, the contractor should have been paid only \$312,500, and HUD should be reimbursed more than \$1.3 million. See the table below.

⁴ The cutover contract task requires the contractor to perform tasks such as conducting a production readiness review for OCFO; providing support and coordination to conduct the go live, which includes executing the production data conversion and tasks as defined in the transition cutover plan; and providing post implementation support, help desk support for production issues, and support for the analysis and evaluation of the PeopleSoft software release after go live.

Total amount paid to the Project contractor	\$1,668,424
Total amount that should have been paid based on work completed by the Project contractor	\$ 312,500
Amount to be reimbursed to HUD	\$1,355,924

OCFO paid the entire amount of the contract task without ensuring that the task had been completed. In September 2011, HUD paid the Project contractor the full amount of \$220,051 for work associated with the contract task to build and unit test ICFS PeopleSoft production environments.⁵ However, one of the required contract deliverables for this task was not received until March 2012 and was not accepted by OCFO until May 2012. Paying the contractor the total price of the contract task before all contract deliverables were received and all completed contract tasks were accepted by HUD could limit OCFO’s ability to enforce the contract and negatively impact the implementation of ICFS.

The Project Deliverable Review Was Inadequate and the Payment Schedule Was Noncompliant

The conditions above occurred because the project deliverable review and approval process used by OCFO officials was not adequate and the payment schedule set up in the contract for the cut-over contract task did not comply with HUD procurement requirements.

The government technical representative did not always verify that the deliverables or services were completed and accepted by HUD before the payment approval. HUD management was negotiating with the Project contractor to change the contract monitoring approach from a “contract deliverable” base to an “outcome deliverable” base. HUD Handbook 2210.3, Procurement Policies and Procedures, REV-9, section 12-6, states that for fixed-price contracts, the government technical representative should verify that all deliverables and services included on the invoice have been inspected and are acceptable. The Project government technical representative approved payments to the contractor once there was evidence that the contractor had started each task. However, contract deliverables were not completed or approved for full payment. The government technical representative did not verify whether the deliverables and services were acceptable before payment.

⁵ The contract task of build and unit test ICFS PeopleSoft production environments requires the contractor to perform tasks such as configuring and validating configuration of production environments and setting up the performance test environment for disaster recovery and the disaster recovery environment for production. The contractor also must conduct unit testing of the production and disaster recovery environments and resolve deficiencies identified.

The partial payment schedule included in the Project contract did not comply with HUD acquisition regulations, which require the contractor to provide deliverables to receive each partial payment. As a result, the Project contractor continued to receive the partial payments if the contract deliverables were in progress, even if contract tasks failed or were incomplete. Section 2452.232-70 of the regulations requires that the partial payment schedule include applicable contract deliverables for each partial payment. Without having specific deliverables associated with each payment on the payment schedule, HUD cannot ensure that the contractor implements the contract tasks as required in the contract and in a timely manner before approving each partial payment. In addition, the partial payment schedule did not include a requirement to withhold a percentage of the contracted amount for each task until the task was completed. The Project contract requires that all partial payments be contingent upon the acceptance of all work completed during the period covered by the partial payment. While the partial payment schedule in the Project contract included the requirement for some contract tasks, the requirement was not included for 42 of 61 contract tasks under the base contract period. As a result, OCFO did not withhold any contract amount to ensure that these tasks were completed before the contractor received the full payment for the cut-over contract task.

Conclusion

OCFO did not properly manage the payments related to data conversion activities of the Project. Specifically HUD did not have a payment schedule that complied with HUD procurement requirements, which led to payments to the contractor without corresponding completed project deliverables. Without properly reviewing and verifying all deliverables and services provided by the contractors, HUD could not ensure that contract requirements would be achieved. As a result, the contractors received a \$1.67 million payment for incomplete contract tasks, when they should have been paid only \$312,500. Also, OCFO cannot ensure all Project objectives are met due to the improper management of the data conversion activities.

Recommendations are addressed to the Office of the Chief Procurement Officer because reimbursement payment issues cannot be addressed by OCFO. The Office of the Chief Procurement Officer has begun the process of recouping the more than \$1.3 million from the Project contractor.

Recommendations

We recommend that the Office of the Chief Procurement Officer:

- 1A. Continue to seek reimbursement of \$1,355,924 from the Project contractor for the contract task of cutover or hold the Project contractor responsible to complete the contract requirement.
- 1B. Ensure that future fixed-price contracts require that a contract deliverable be associated with each payment on the partial payment schedule.
- 1C. Ensure that future fixed-price contracts with partial payment schedules include a requirement to withhold a percentage of the contracted amount for each task until the task has been completed.

SCOPE AND METHODOLOGY

The audit was performed between February and June 2012 at HUD headquarters, Washington, DC. Data reviewed were for the period 2004, the initiation of the Project, to July 2012, after the base period of the contract ended. Our overall objective was to evaluate whether HUD was ready to move forward with the full implementation of ICFS. During this review, we noted incorrect payments to the contractor for some contract tasks. To accomplish our objective of reviewing HUD's management of payments related to data conversion activities, we

- Used Office of Management and Budget Circular A-127, HUD acquisition regulations, and HUD Handbook 2210.3, Contractor Costs and Payments, as guidance.
- Conducted interviews with staff and contractors from OCFO and the Office of the Chief Procurement Officer and reviewed the Project contract.
- Obtained an understanding of the data conversion specifications and the Project deliverable and approval process.
- Reviewed the contract and supporting documentation for data conversion methodologies.
- Obtained an understanding of the contract payment approval process and contract payment status of data conversion related contract tasks.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

INTERNAL CONTROLS

Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

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

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined that the following internal controls were relevant to our audit objective:

- Up-to-date written policies and procedures to ensure that data conversion and interfaces were complete and valid.
- Compliance with Federal requirements.
- Design and implementation of policies and procedures.

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

Significant Deficiency

Based on our review, we believe that the following item is a significant deficiency:


OCFO lacked adequate controls to ensure that payments to the Project contractor were correct. Further, OCPO did not ensure that the partial payment schedule was properly set up in the contract (finding 1).

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

	 <p>U.S. Department of Housing and Urban Development Washington, D.C. 20410</p> <p>CHIEF PROCUREMENT OFFICER NOV 21 2012</p> <p>MEMORANDUM FOR: Hanh T. Do, Director, Information Systems Audit Division,</p> <p>FROM: Jemine A. Bryon, Chief Procurement Officer, HUD</p> <p>SUBJECT: Response to Audit of Incorrect Payments to the HIFMIP Project Contractor</p> <p>We have reviewed the OIG's audit report on HUD's implementation of the Integrated Core Financial System as it relates to contract activity. Below you will find responses to the recommendations proposed to the Office of the Chief Procurement Officer.</p> <p>Response to Recommendation 1A: A payment adjustment of \$1,355,924 was completed during OCPO's performance review of the contract. No further action relating to this recommendation is needed.</p> <p>Response to Recommendation 2A: As appropriate, OCPO will ensure future payment schedules are associated with deliverables/outcomes.</p> <p>Response to Recommendation 2A: As appropriate, OCPO will ensure future fixed-price contracts with partial payment schedules maximize opportunities for withholding a percentage against tasks.</p> <p>Thank you.</p> <p><i>Visit our web page at http://www.hud.gov/offices/cpo/index.cfm</i></p>
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Comment 1

Comment 2

Comment 3

OIG Evaluation of Auditee Comments

Comments 1, 2, and 3

OIG concurs with OCPO comments (Auditee comments to 1A, 2A, 2A correspond to recommendations 1A, 1B, and 1C)