



Management Controls, Systems, and Compliance With Laws and Regulations

Federal Managers' Financial Integrity Act

The Federal Managers' Financial Integrity Act (FMFIA) requires agencies to establish management controls over their programs and financial systems. Throughout the year, VA managers monitor and improve the effectiveness of management controls associated with their programs and financial systems. The results of monitoring and conducting other periodic evaluations provide the basis for the Secretary's annual assessment of and report on management controls. VA managers are required to identify material weaknesses relating to their programs and operations pursuant to sections 2 and 4 of the FMFIA as defined:

- Section 2 requires agencies to assess internal controls necessary to ensure compliance with applicable laws and regulations; protect against loss from waste, fraud, and abuse; and ensure receivables and expenditures are properly recorded.
- Section 2 also requires management's assessment of internal control over financial reporting.
- Section 4 requires agencies to assess nonconformance with governmentwide financial systems requirements.

Management Assurances

Department managers continue to take responsibility for establishing and maintaining effective internal controls over financial integrity and financial reporting, including safeguarding assets and complying with applicable laws and regulations. During 2007, the Former Secretary of Veterans Affairs maintained his leadership role in stressing that strong internal controls will enhance the Department's stewardship of taxpayers' assets and programs.

Management conducted its assessment of the effectiveness of internal controls over operations and compliance with applicable laws and

regulations in accordance with the Federal Managers' Financial Integrity Act (FMFIA) and OMB Circular A-123, Management's Responsibility for Internal Control. After reviewing the results of the assessments outlined in the Statements of Written Assurance provided by the Under Secretaries, Assistant Secretaries, and other Key Officials, the Acting Secretary of Veterans Affairs provided a statement of qualified assurance. Four material weaknesses: "IT Security Controls," "Financial Management System Functionality" (previously identified as "Lack of an Integrated Financial Management System"), "Financial Management Oversight" (previously identified as "Operational Oversight"), and "Retention of Computer Generated Detail Records in Benefits Delivery Network (BDN) System - VBA," were identified as material weaknesses under FMFIA.

In addition, the Secretary provided a qualified assurance statement reflecting the status of internal controls over financial reporting for 7 of 11 key business processes as of June 30, 2007. VA conducted a limited scope assessment as of June 30, 2007, on the effectiveness of internal controls over financial reporting for six key business processes: Revenue Management; Property, Plant & Equipment; Budgetary Resources; Procurement Management; Risk Management; and Benefits Management (partial). Information Technology Management was also assessed, as it relates to these six processes. Assessment of internal controls over financial reporting for Funds Management and Financial Reporting was completed in 2006. Based on the results of VA's limited scope assessment, no material weaknesses were identified. VA can provide a qualified statement of assurance that internal controls over financial reporting were operating effectively.



November 15, 2007

Statement of Qualified Assurance

The Department of Veterans Affairs' (VA) management is responsible for establishing and maintaining effective internal control and financial management systems that meet the objectives of the Federal Managers' Financial Integrity Act (FMFIA). VA is able to provide a qualified statement of assurance that the internal controls and financial management systems meet the objectives of FMFIA, with the exception of four material weaknesses. The details of the exceptions are provided within Part I, "Management Controls, Systems, and Compliance with Laws and Regulations," and the "Summary of Financial Statement Audit and Management Assurances" tables are shown in the beginning of Part IV, "Other Accompanying Information," in this report.

VA conducted its assessment of the effectiveness of internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations in accordance with OMB Circular A-123, *Management's Responsibility for Internal Control*. Based on the results of this evaluation, VA identified four material weaknesses in its internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations as of September 30, 2007. Other than the exceptions noted, the internal controls were operating effectively, and no other material weaknesses were found in the design or operation of internal controls.

In addition, VA conducted a limited scope assessment of the effectiveness of internal control over financial reporting, which includes safeguarding of assets and compliance with applicable laws and regulations, in accordance with the requirements of OMB Circular A-123, Appendix A. Based on the results of the assessment of key business processes tested during FY 2007, and other than the material weaknesses noted above, VA's internal controls over financial reporting are operating effectively and no material weaknesses were identified as of June 30, 2007.

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Gordon H. Mansfield
Acting



Summary of Auditor's Internal Control Assessment

The auditors' report on internal controls reported four material weaknesses: "Financial Management System Functionality," "Information Technology (IT) Security Controls," "Financial Management Oversight," and "Retention of Computer Generated Detail Records in Benefits Delivery Network (BDN) System – VBA." Under "Financial Management System Functionality," the auditors identified continuing difficulties with the legacy systems related to the reliable, timely, and consistent preparation, processing, and analysis of financial information for VA's consolidated financial statements. In the IT material weakness, the auditors noted progress in certain areas, but reported that legacy IT infrastructure and longstanding security control weaknesses due to the lack of effective implementation and enforcement of an agency-wide information security program continue to place VA's program and financial data at risk. The third material weakness, "Financial Management Oversight," identified the need for enhanced management oversight in the following areas:

- Accrued Services Payable and Undelivered Orders
- Accounts Receivable
- Property, Plant and Equipment
- Environmental and Disposal Liabilities
- Payroll Agreed-Upon Procedures Reporting
- Accrual for Unbilled Receivables and Allowance for Adjusting Entries and Contractual Adjustments
- Adjusting Entries and Reconciliation Review
- Compensation and Pension Actuarial Liability

The new material weakness, "Retention of Computer Generated Detail Records in Benefits Delivery Network (BDN) System – VBA," reported the inability to provide detail computer transactions to support amounts reported in the financial statements and to reconcile subsidiary

system balances to the core financial system due to failure to retain computer generated details beyond 60 to 90 days.

To address the Department's material weakness, Financial Management System Functionality, VA is continuing its efforts to develop the Financial & Logistics Integrated Technology Enterprise (FLITE) program. The program has two primary components, a logistics and asset management component, referred to as the Strategic Asset Management (SAM) project, and a financial management system component, referred to as the Integrated Financial Accounting System (IFAS). In 2007 the Department also continued enhancement of the Hyperion Financial Management reporting system to improve the preparation, processing, and analysis of financial information, adding additional reports and features, and continued implementation of a data warehouse to assist in financial reporting.

In addition, VA continues, through its Financial Reporting Data Warehouse, to analyze and improve the major interfaces to and from its core financial system, the Financial Management System (FMS). Final resolution of this weakness is a multi-year effort.

Additional focus was placed in 2007 on the Financial Management Oversight material weakness due to the expansion of this significant deficiency to other fiscal areas in VA (expanded beyond simply VHA as described in 2006). VA developed and implemented a detailed remediation action plan to address the resolution of this material weakness. VA financial management made improvements throughout the year in providing additional and clarifying financial policies and procedures to VA's fiscal community, particularly in the area of internal controls. VHA's Business Process Improvement Committee (BPIC) continued to work toward improving VHA's internal controls and reforming VHA business processes to improve financial performance.



The auditors’ report on compliance with laws and regulations, also prepared as a result of the 2007 financial statement audit, determined that the Department did not substantially comply with the Federal Financial Management Improvement Act (FFMIA) requirements as it relates to “Financial Management System Functionality,” Information Technology (IT) Security Controls,” and “Retention of Computer Generated Detail Records in BDN System - VBA” material weaknesses. VA was also noncompliant with the Debt Collection Improvement Act and with USC Title 5, 552A, “Records Maintained on Individuals.”

Progress on Material Weaknesses

VA managers continue to make progress in correcting existing material weaknesses. The 2007 Consolidated Financial Statements Audit Report disclosed four material weaknesses. Management identified four of these same weaknesses: “IT Security Controls,” “Financial Management System Functionality,” “Financial Management Oversight,” and “Retention of Computer Generated Detail Records in Benefits

Delivery Network (BDN) System - VBA,” as weaknesses under FMFIA. At the end of 2006, three audit-related material weaknesses¹ (Information Technology Security Controls, Lack of Integrated Financial Management System (now titled Financial Management System Functionality), and Operational Oversight (now titled Financial Management Oversight) were carried forward into 2007. These same weaknesses will also be carried forward into 2008 along with the new weakness, “Retention of Computer Generated Detail Records in Benefits Delivery Network (BDN) System - VBA.” (Note: Material weaknesses identified under FMFIA are the same as the audit-related material weaknesses and will be corrected using the same remediation plan.)

¹The use of the term “material weakness” should not be confused with use of the same term by government auditors to identify management control weaknesses, which, in their opinion, pose a risk or threat to the internal control systems of an audited entity, such as a program or operation. Auditors are required to identify and report those types of weaknesses at any level of operation or organization, even if management of the audited entity would not report the weaknesses outside the agency.

The four audit-related material weaknesses are shown in the table below, which provides the current status of the Department’s material weaknesses. Additionally, the four material weaknesses identified by management in 2007 are shown in the table.

Audit Material Weaknesses or Weaknesses Identified by Management

Description	Current Status	Resolution Target Date
<p>Information Technology Security Controls (Audit/FMFIA Section 4 weakness)– VA’s assets and financial data are vulnerable to error or fraud because of weaknesses in information security management,</p>	<p>The Data Security—Assessment and Strengthening of Controls Program was established to correct deficiencies and eliminate vulnerabilities in the area of information security. This over-arching program is a cross-cutting effort to complete hundreds of tasks that are necessary to remediate long-standing security weaknesses.</p> <p>In 2007, Handbook 6500, “Information Security Program,” was published and will provide the foundation for a comprehensive information security program throughout VA. Tracking and reporting of audit finding remediation activities have been increased, and 145 security assessments were performed by the newly-created Office of IT Oversight and Compliance.</p>	<p>2009</p>



Description	Current Status	Resolution Target Date
<p>access to controls and monitoring, and physical access controls.</p>		
<p>Financial Management System Functionality – (Audit/FMFIA Section 4 weakness)– Difficulties exist in the preparation, processing, and analysis of financial information to support the efficient and effective preparation of VA’s consolidated financial statements.</p> <p>– Components of certain feeder systems and financial applications are not fully integrated with the core Financial Management System.</p>	<p>To address the Department’s material weakness, Financial Management System Functionality, VA is continuing its efforts to develop the Financial & Logistics Integrated Technology Enterprise (FLITE) program. FLITE will integrate many disparate systems, standardize functional processes, and modernize the information technology environment supporting financial and logistics management within VA. The program has two primary components, a logistics and asset management component, referred to as the Strategic Asset Management (SAM) project, and a financial management system component, referred to as the Integrated Financial Accounting System (IFAS).</p> <p>In 2007 VA continued the prerequisite planning for the FLITE program, which included establishing and implementing the FLITE governance framework, developing the FLITE program baseline cost estimates and integrated master schedule, documenting business requirements and business processes, establishing an acquisition strategy, determining the COTS solution for the SAM component of FLITE, conducting a stakeholder analysis and communications needs assessment for the Organizational Change Management Strategy, and performing a full analysis on lessons learned from CoreFLS to monitor during the FLITE project lifecycle. In 2008 VA expects to award the SAM Integration contract and initiate the SAM pilot at the Milwaukee VAMC. The pilot will attain Initial Operating Capability of the SAM system. In addition, IFAS will follow the financial management line of business (FMLoB) guidance to compete and award the IFAS contract and take steps to initiate the IFAS pilot in FY 2009. The pilot will validate the business requirements, test any applicable interfaces, and ensure proper security and accessibility of data. The pilot will attain Initial Operating Capability of the IFAS system.</p> <p>Under the FLITE umbrella as an interim initiative, VA is also continuing to implement a data warehouse to capture transaction details from selected interfacing systems throughout the Department and the corresponding core Financial Management System (FMS) transactions. Under this initiative, VA is analyzing financial system interfaces to identify weaknesses and deficiencies and define corrective</p>	<p>2012</p>



Description	Current Status	Resolution Target Date
	<p>requirements. This initiative will simplify the reconciliation between the interface and FMS. It will also ensure a clear audit trail exists for financial transactions that interface with the core financial system and ensure all interfacing systems to the core financial system are A-127 compliant. In 2007, the data warehouse for two of the targeted interfaces, PAID and Loan Service and Claims (LS&C), were implemented as scheduled.</p> <p>To address the weakness in the preparation of VA’s financial statements, in 2006 the Department successfully implemented the Hyperion Financial Management reporting system, commercial off-the-shelf (COTS) software to improve the preparation, processing, and analysis of financial information. The system was used to produce the 2007 quarterly and consolidated financial statements. This system is now completely producing VA consolidated financial statements using a standardized and repeatable process. The cumbersome legacy process to produce the statements has been retired.</p>	
<p>Financial Management Oversight – (Audit/FMFIA Section 2 weakness)– Internal controls and reconciliation processes were not performed consistently or completely.</p>	<p>In 2007 VA placed additional focus on the Financial Management Oversight material weakness due to the expansion of this significant deficiency to other fiscal areas in VA (expanded beyond simply VHA as described in 2006). VA developed and implemented a detailed remediation action plan to address the resolution of this material weakness. VA financial management made improvements through the year in providing additional and clarifying financial policies and procedures to VA’s fiscal community, particularly in the area of internal controls. VHA’s Business Process Improvement Committee (BPIC) continued to work toward improving VHA’s internal controls and reforming VHA business processes to improve financial performance. Examples of the actions taken in the past year include the following:</p> <ul style="list-style-type: none"> • VHA developed and issued an extensive desk guide for processing non-MCCF accounts receivable; • VBA developed an Audit Management Directive and Reconciliation Directive; • VA’s Office of Finance began a comprehensive initiative to rewrite and update all VA financial policies and procedures (3-year effort). <p>These, as well as other numerous efforts, are continuing into 2008 to resolve this material weakness.</p>	<p>2009</p>



Description	Current Status	Resolution Target Date
<p>Retention of Computer Generated Detail Records in Benefits Delivery Network (BDN) System - VBA (Audit/FMFIA Section 4 weakness)– Certain computer generated transaction details from the BDN system are only retained for approximately 60 to 90 days.</p> <p>– Supporting detail is not available to substantiate amounts recorded on financial statements.</p>	<p>Newly identified</p>	<p>TBD</p>

Summary of Management’s Assessment of Internal Controls

Managers assessed the programs for which they are responsible to ensure internal controls are in place over the effectiveness and efficiency of operations and compliance with laws and regulations. As a result of their assessments in this area, four material weaknesses were identified and are shown in the “Summary of Auditors’ Internal Control Assessment” section.

Management Control Weaknesses

In 2007, there were no material weaknesses carried forward from 2006 by management. By the end of FY 2007, one material weakness, “Financial Management Oversight,” was identified under Section 2, as a result of management’s assessment during the fiscal year.

Management’s assessment of internal controls over non-conformances identified two material non-conformances under Section 4, “IT Security Controls,” and “Financial Management System Functionality.” Based on the results of the audit, a new system-related material weakness, “Retention of Computer Generated Detail Records in Benefits Delivery Network (BDN) System - VBA” was also identified in Section 4 as a material non-conformance under FMFIA.

The revised OMB Circular A-123 titled Management’s Responsibility for Internal Control, Appendix A, is intended to strengthen the requirements for conducting management’s assessment of internal control over financial reporting.



In 2006, VA identified 11 key business processes that impact the internal controls over financial reporting. VA plans to perform an assessment of internal controls for these key business processes over a 3-year cycle. During the second-year cycle (2007), VA selected six business processes to test: Revenue Management; Property, Plant & Equipment; Budgetary Resources; Procurement Management; Risk Management; and Benefits Management (partial). Information Technology Management was also reviewed specifically as it relates to the six key business processes.

As a result of testing these key business processes, 27 findings were identified in the “Findings and Recommendations for Internal Controls Improvements Report” issued by Grant Thornton for each of the processes. The finding regarding Capitalized equipment was identified as a new significant deficiency. This finding, as well as the finding regarding Intragovernmental Transactions, are further described in the chart below.

FY 2007 Significant Deficiencies Identified in the Findings and Recommendations for Internal Controls Improvements Report

Findings	Recommendations	Remediation Date
Capitalized equipment could not be located.	Develop a process to monitor Property, Plant & Equipment at the Medical Centers to ensure it is being properly accounted for and inventoried. Provide training to end-users on the current and revised policies and procedures.	FY 2008
Intragovernmental Transactions	Take the appropriate measures to implement a process to extract trading partner data from its FMS, including an improved query capability that enables meaningful analysis of its trading partner data. Also, VA needs to implement a process to sample its transactions to ensure trading partner “identifiers” are being entered into VA’s FMS correctly when a transaction originates, reducing the likelihood that trading partner variances are being caused by VA.	FY 2008; Completion date deferred from FY 2007 due to expansion of scope to more robust system able to fully resolve issue and ensure all transactions are captured.

Federal Financial Management Improvement Act

The Federal Financial Management Improvement Act (FFMIA) requires agencies to have systems that generate timely, accurate, and useful information with which to make informed decisions and to ensure accountability on an ongoing basis. The Department faces challenges in building and maintaining financial

management systems that comply with FFMIA. Under FFMIA, VA is substantially compliant -- with the exception of federal financial management systems requirements. VA initiated a remediation program in 2005 to eliminate the existing material weakness--Lack of an Integrated Financial Management System (now referred to as Financial Management System Functionality). This new program is



called FLITE--the goal of which is to correct financial and logistics deficiencies throughout the Department. In 2007 VA continued the prerequisite program planning, which included establishing and implementing the FLITE governance framework, developing the FLITE program baseline cost estimates and integrated master schedule, documenting business requirements and processes, establishing an acquisition strategy, determining the COTS solution for the SAM component of FLITE, conducting a stakeholder analysis and communications needs assessment for the Organizational Change Management Strategy and performed a full analysis on lessons learned from CoreFLS to monitor during the FLITE project lifecycle. In 2008 VA expects to award the SAM Integration contract and initiate the SAM pilot at the Milwaukee VAMC. The pilot will attain Initial Operating Capability of the SAM system. In addition, IFAS (the financial component of the FLITE program) will follow the FMLoB guidance to award the IFAS contract and take steps to initiate the IFAS pilot in FY 2009. The pilot will validate the business requirements, test any applicable interfaces, and ensure proper security and accessibility of data. The pilot will attain Initial Operating Capability of the IFAS system. This effort is being led by the Chief Financial Officer (business requirements) and the Chief Information Officer (technical solution). The multi-year initiative is highly complex and impacts VA-wide financial reporting systems.

In 2007 the Department continued enhancement of the Hyperion Financial Management reporting system to improve the preparation, processing, and analysis of financial information, adding additional reports and features, and continued implementation of a data warehouse to assist in financial reporting.

In 2007 VA's Internal Controls Service within the Office of Business Oversight completed a series of reviews to examine the interfaces between VA's core FMS and its material feeder systems. Seven systems were reviewed to

identify the systems' compliance with the requirements of FFMIA, as implemented by OMB Circular A-127, Financial Management Systems. VA's Personnel and Accounting Integrated Data (PAID), Veterans Health Information Systems and Technology Architecture Accounts Receivable (Vista AR), Education, Loan Guaranty, Vista, IFCAP, and Vista Fee interfaces were found to be *Substantially Compliant*. The review of the Insurance General Ledger system interface identified opportunities to enhance the functionality of the system to better address requirements for internal control and effective financial management.

In 2007 the data warehouse for two of the targeted interfaces, PAID and LS&C interfaces, has been implemented as scheduled.

Federal Information Security Management Act

The Federal Information Security Management Act (FISMA) provides the framework for securing the federal government's information technology. All agencies covered by the Paperwork Reduction Act must implement the requirements of FISMA and report annually to the Office of Management and Budget and Congress on the effectiveness of the agency's security programs. The reports must also include independent evaluations by the agency Inspector General. VA is aware of the vulnerability of its assets and financial data to error and/or fraud and is in the process of correcting the Information Technology Security Controls material weakness. VA has now implemented a cycle of continuous monitoring, testing, and remediation of vulnerabilities. Staff uses a database tool to help ensure that all vulnerabilities are addressed. In 2008 VA will certify and accredit over 600 of its systems.

In addition, VA has developed the Data Security – Assessment and Strengthening Controls Program, a plan to correct deficiencies and eliminate vulnerabilities in information security. The over-arching program is a cross-



cutting effort to complete hundreds of tasks that are necessary to remediate long-standing security weaknesses. The plan places emphasis in the four areas that make up VA’s IT Security Controls material weakness: Access Controls, Segregation of Duties, Service Continuity, and Change Controls.

The establishment of VA’s IT appropriation and the realignment of IT, including the information

security staff, creates the centralized environment that promotes the command and control necessary to rectify longstanding problems. The Secretary has also provided the delegation of authority that makes clear the authority of the Assistant Secretary for Information and Technology (CIO) to direct the remediation of IT security deficiencies.

IG Act Amendments of 1988

The Inspector General Act requires management to complete all final actions on recommendations within 1 year of the date of the Inspector General’s final report. Department-wide, 15 reports have been pending final action for over 1 year. Based on reporting requirements, the following table summarizes the number of IG reports and the dollar values associated with Questioned Costs and Funds to Be Put to Better Use.

Questioned Costs and Funds to Be Put to Better Use Reporting Period October 1, 2006—September 30, 2007 (dollars in millions)				
	Questioned Costs		Funds to Be Put to Better Use	
	Reports	Value	Reports	Value
Balance 9/30/06	0	\$0	0*	\$0*
New Reports	2	\$5.6	8	\$114.7
Total	2	\$5.6	8	\$114.7
Completed	2	\$5.6	8	\$114.7
Balance 9/30/07	0	\$0	0	\$0

* Note: The numbers listed for Balance 9/30/06 under “Funds to Be Put to Better Use” were revised from last year’s reported figures in accordance with IG Act reporting requirements.

Source: *Compliance with the IG Act Amendments of 1988* section reported by the Office of Inspector General, Operational Support Division.

Prompt Payment Act

VA continued to enhance its vendor payment processes throughout 2007. Interest payments VA-wide improved by \$25,400 (from \$858,500 to \$833,100) – a 3.0 percent improvement over 2006 levels, largely attributable to the centralization of VHA payments at the VA Financial Services Center (FSC) in Austin, Texas. Further, 2007 interest paid per million dollars disbursed improved more than 15 percent from \$99 per million in 2006 to \$84 per million in 2007. At the same time, VA earned nearly 92

percent (\$4.3 million) of its available discounts. VA also continued to gain efficiencies and improve performance through an initiative started in 2004 to centralize VHA vendor payment activities at the FSC. Through this centralization, VA strengthened its focus on identifying and preventing vendor payment errors. The FSC also enhanced audit recovery efforts over improper/duplicate vendor payments. The FSC reviews VA vendor payments daily to systematically identify, prevent, and recover improper payments made to



commercial vendors. Current payment files are matched to identify and, where possible, prevent duplicates prior to payment. Also, payments from prior fiscal years are matched to identify potential duplicate payments for further analysis, assessment, and, as appropriate, collection. The FSC also contracted with a commercial recovery audit firm to review prior fiscal year payment files in an effort to identify any additional improper/duplicate payments for recovery.

The FSC staff also reviews vendor payments to identify and collect improper payments resulting from duplicate incentive award payments, erroneous interest penalties, service charges, and sales taxes. This initiative recovered over \$338,000 during 2007 for reuse by VA entities. Overall, collections of improper payments and the recovery of unapplied vendor statement credits totaled nearly \$3.0 million. Improved payment oversight also enabled VA to identify and cancel nearly \$10.4 million in potential improper payments prior to disbursement. Since inception of the FSC audit recovery effort in 2001, VA has recovered \$21.3 million in improper payments and prevented the improper payment of another \$32.9 million.

The FSC successfully implemented Optical Character Recognition (OCR) technology for the approximately one million commercial vendor payments processed annually. OCR technology improved payment processing cycle times and payment accuracy and timeliness, and enhanced customer service. In conjunction with the OCR project, the FSC successfully implemented a business rules engine that utilizes Microsoft .Net™ technology to automate invoice processing procedures. Benefits from the implementation include reduced manual processing, standardized application of operating procedures, improved productivity, and reduced errors in processing.

During 2007 the Department aggressively used the governmentwide commercial purchase card program. Over 4.2 million transactions were processed, representing \$2.6 billion in

purchases. As a result of VA's daily electronic billing and payment process for centrally billed accounts, VA earned over \$42 million in refunds, compared to \$37 million during the same period in 2006. These refunds are returned to VA entities for use in veterans programs. The increase in refunds is attributed to expanded use of the card and normal increases in the cost of products purchased.

VA's Fee Basis purchase card program automates Health Care Fee Basis payments, eliminates processing of paper checks, and earns VA additional purchase card refunds. During 2007 the number of Fee Basis purchase card transactions exceeded 280,000 and were valued at \$98 million in payments, earning VA almost \$1.6 million in additional refunds compared to 824,000 during 2006.

VA's Prime Vendor Payment System automates payments under a nationwide prime vendor centralized purchasing contract. During 2007, 135 VA medical centers used the Prime Vendor Payment System to electronically process over 458,000 transactions worth over \$3.5 billion.

VA's Travel Management Centers (TMC) serve veterans and employees who travel frequently. The billings are transmitted electronically from each TMC, and payment is sent daily through the Department of the Treasury's Electronic Certification System. During 2007 the travel management program processed over 164,000 transactions, disbursed payments of over \$28 million, and earned over \$339,000 in refunds.

The FSC staff continued to provide vendor payment history on the Internet. Currently, the Vendor Inquiry System (VIS) Internet application stores over 3 years of information on invoices. Once vendors complete an authentication process, they can access a secure Web site to view payment information for their company. Currently there are over 13,234 active registered vendors who made over 472,086 requests in 2007 and over 1.8 million requests since VIS's inception in April 2003. The VIS



provides FSC vendors an easy-to-use tool for immediate access to their payment information 24 hours a day. The VIS has also improved customer service efficiency of FSC staff by handling many routine inquiries and freeing staff to work the more difficult issues for customers.

Registered users of VIS have the ability to submit electronic invoices directly to the FSC. Vendors complete easy-to-use forms to create their invoices and can manage and track them. This online system provides the vendors with a list of valid purchase orders, virtually eliminating the number one error that causes payment delays. Errors identified by the system are immediately returned to the VIS user, who can instantly correct them prior to submission. This prevents payment delays and results in quicker and more accurate vendor payments. Since our initial opening of VIS, we have processed over 27,047 invoices totaling \$546 million.

The FSC also continued to improve the Intranet online invoice certification process that allows invoices to be certified electronically by VA facilities and scheduled for payment. Site Administrators now have the ability to change purchase order numbers within the On Line Certification System (OLCS) application, route invoices to the appropriate officials for approval, and expedite processing for utility payments. VA's On Line Certification System (OLCS) allows the FSC to notify certifying officials via e-mail of any invoice requiring payment certification. Through the Intranet, the certifying official can view, certify, and forward the invoice to the FSC for payment processing, reducing the processing time to hours rather than days. The FSC completed the centralization of certified and matched payments throughout VA in 2006 and implemented OLCS at all facilities, bringing the number of OLCS users to more than 10,000 VA employees.

Improper Payments Information Act of 2002 (Summary of Implementation Efforts for FY 2006 and Agency Plans for FY 2007 through 2009)

Overview

VA reviewed the requirements of the Improper Payments Information Act (IPIA) of 2002 to identify those programs that are susceptible to significant erroneous payments. After completing the review, VA performed risk assessments for all programs, which account for approximately the entire VA budget. Statistical samplings were performed on all required programs to estimate improper payments.

All programs not reported had estimated improper payments of less than \$10 million; thus, no report was required for these programs. Dependency and Indemnity Compensation (DIC) is one of the programs previously identified in the former Section 57 of OMB Circular A-11, Preparation and Submission of Budget Estimates, but is included in the Compensation Program. The remaining programs either had estimated improper payments exceeding \$10 million and/or were programs previously identified in the former Section 57 of OMB Circular A-11. These include the Compensation, Pension, Education, Insurance, Loan Guaranty, Non-VA Care Fee, and Vocational Rehabilitation & Employment programs. Although the Insurance program was one of the programs identified in Section 57 of OMB Circular A-11, the risk assessment for the program is low. Because the Insurance program does not meet the 2.5 percent or \$10 million threshold in annual erroneous payments, OMB no longer requires an annual report in the PAR. Because the Vocational Rehabilitation & Employment (VR&E) program has not met the reporting requirements for the past 2 years, VA requested relief from future annual reports for the program and was granted relief from annual reporting until 2010. Further details are provided in Part IV of this report.



Accomplishments

VA's Assistant Secretary for Management/Chief Financial Officer (CFO) is the designated senior official responsible for implementing IPIA. The CFO is responsible for establishing policies and procedures to assess VA program risks of improper payments, taking actions to reduce those payments, and reporting the results of those actions to VA management. Managers of all programs identified for review are aware of the importance of the IPIA.

All programs identified for review completed the risk assessment or completed statistical samplings in 2007 for 2006 data in accordance with VA's IPIA plan. VA also identified under- and over-payments by program, and provided program assessments and corresponding steps to prevent future erroneous payments in accordance with IPIA. Acceleration in identifying fugitive felons and the agreement between VA and many states allowed VA to identify errors and assisted in identifying erroneous payments.

VA met the improper payment reduction targets for Compensation, Pension, and Vocational Rehabilitation & Employment. VA did not meet the reduction target in the Education and Loan Guaranty programs. All programs met or exceeded the recovery targets used for 2007.

Plans to Accomplish

VA aims to reduce the amount of erroneous payments in all programs. Efforts are still ongoing to standardize training materials for all field stations to improve claims processing performance and to develop and automate claims processing for the Education program. The Pension program consolidates the processing of all pension maintenance workload to the Pension Maintenance Centers in order to improve the quality and timeliness of pension processing and to focus training in these areas. The Vocational Rehabilitation & Employment program established a national quality assurance team to monitor the errors annotated in the quality assurance reviews and track the corrective actions

taken on identified errors. The Loan Guaranty (LGY) program will continue to conduct 100 percent post-payment reviews of all Specially Adapted Housing (SAH) grant payments. In addition, LGY has developed a statistical quality control schedule for the SAH process, which will provide additional opportunity for review of the grant process, including grant payments.

Financial Management Systems Framework

Overview

The Department's strategy, defined about 13 years ago, is based on goals to replace outdated and noncompliant systems with more modern, commercial off-the-shelf (COTS) systems which meet Office of Federal Financial Management core financial system requirements. This strategy was enhanced to incorporate business process reengineering in the requirements, acquisition, and development and implementation phases of projects.

The Office of Business Oversight's Internal Controls Service provides the CFO with independent review and advisory services designed to add value and improve the acquisition, development, maintenance, and retirement of VA financial systems. The scope of this work is to determine whether the Department's financial systems comply with the FFMIA, as implemented by OMB Circular A-127.

The Internal Controls Service conducts reviews of financial systems and processes to determine compliance with OMB Circular A-127, conduct management-directed program activities and system management reviews of project management processes and results, and monitor corrective action to address deficiencies identified in reviews.

In 2007 Internal Controls Service conducted four OMB Circular A-127 compliance reviews as part of a coordinated effort with the Office of Financial Business Operations to develop a plan to remediate specific weaknesses associated with



integrated financial reporting capability and data quality and timeliness provided by legacy systems. Four additional A-127 reviews were completed in conjunction with the Department's OMB Circular A-123 Appendix A program. VA is addressing findings and implementing recommendations from these reviews.

VA's updated financial systems inventory provides details on all major financial and mixed systems. The major financial system initiatives funded by the Department over the last 14 years to achieve VA's strategic goals have included the following:

- The Financial Management System (FMS) was designed to replace VA's 1970's central accounting system. In the FMS initiative, completed in 1995, VA successfully met its stated objectives and implemented FMS as its single, core accounting system based on a certified COTS, Joint Financial Management Improvement Program (JFMIP)-compliant system with interfaces to all other VA payment and accounting systems. In the succeeding, post-implementation years, VA completed several studies and determined there were remaining inefficiencies in the overall financial management processes, areas of noncompliance in our mixed systems, and new mission business requirements that could not be supported economically in the current systems. Difficulties were also cited by auditors related to the preparation, processing, and analysis of financial information in the preparation of VA's consolidated financial statements. Actions taken in 2007 satisfactorily addressed this weakness.
- VA initiated a second multi-year initiative in 2005 to eliminate the existing material weakness—Lack of an Integrated Financial Management System (now referred to as Financial Management System Functionality). This new program is referred to as FLITE—the goal of which is to implement an agency-wide integrated

financial management system (core and mixed feeders) and to correct financial and logistics deficiencies throughout the Department.

- VA continues to move forward in the consolidation of payroll services to the Defense Finance Accounting Service (DFAS), which is included in the President's Management Agenda for Improving Internal Efficiencies and Effectiveness.

Following the success of the first migration of Title 5 employees to DFAS in August 2006, the second migration occurred in October 2007 and included additional Title 5 employees. Extensive system changes are being made to VA's legacy system as well as DFAS' in preparation for additional migrations to accommodate the special pay provisions that apply only to Title 38 employees. Complete migration of VA's payroll services to DFAS is tentatively scheduled for February 2009.

VA's financial system recent accomplishments as well as plans for the next 5 years are detailed as follows.

Financial Management System (FMS) Accomplishments and Plans

VA continued production support and maintenance of FMS during 2007. VA will need to continue operation of FMS as the core accounting system until a suitable replacement is available.

In 2007 the Department continued enhancement of the Hyperion Financial Management reporting system to improve the preparation, processing, and analysis of financial information, adding additional reports and features, and continued implementation of a data warehouse to assist in financial reporting.

Additionally, VA continues to analyze and improve the major interfaces to and from FMS in an effort to improve integration among the



various financial and mixed systems. This effort will assist with the remediation of Financial Management System Functionality material weakness, as well as improve the overall system architecture in preparation for the next generation financial system being planned for in the FLITE effort.

FLITE Accomplishments and Plans

To address the Department's material weakness, Financial Management System Functionality, VA is continuing its efforts in developing the FLITE program. FLITE will integrate many disparate systems, standardize functional processes and modernize the information technology environment supporting financial and logistics management within VA. The program has two primary components, a logistics and asset management component referred to as the SAM project, and a financial management system component, referred to as the IFAS.

In 2007 VA continued the prerequisite planning for the FLITE program, which included establishing and implementing the FLITE governance framework, developing the FLITE program baseline cost estimates and integrated master schedule, documenting business requirements and business processes, establishing an acquisition strategy, determining the COTS solution for the SAM component of FLITE, conducting a stakeholder analysis and communications needs assessment for the Organizational Change Management Strategy, and performed a full analysis on lessons learned from CoreFLS to monitor during the FLITE project lifecycle. In 2008 VA expects to award the SAM Integration contract and initiate the SAM pilot at the Milwaukee VAMC. The pilot will attain Initial Operating Capability of the SAM system. In addition, the IFAS (financial component of the FLITE program) will follow the FMLoB guidance to compete and award the IFAS contract and take steps to initiate the IFAS pilot in FY 2009. The pilot will validate the business requirements, test any applicable interfaces, and ensure proper security and

accessibility of data. The pilot will attain Initial Operating Capability of the IFAS system.

Under the FLITE umbrella as an interim initiative, VA is also continuing to implement a data warehouse to capture transaction details from selected interfacing systems throughout the Department and the corresponding core FMS transactions. Under this initiative, VA is analyzing financial system interfaces to identify weaknesses and deficiencies and define corrective requirements. This initiative will simplify the reconciliation between the interface and FMS. It will ensure a clear audit trail exists for financial transactions that interface with the core financial system and ensure all interfacing systems to the core financial system are A-127 compliant.

In 2007 the data warehouse for two of the targeted interfaces, PAID and Loan Service and Claims (LS&C), was implemented as scheduled.

PAID Accomplishments and Plans

VA continued production support and maintenance of PAID during 2007 in support of Federal-wide programs such as Health Savings Allotments, and changing child support payments from paper to electronic payments. System changes were also completed to implement legislative changes that affected Title 38 employees such as Nurses Special Pay and changes in how lump sum payments for separating employees are computed.

VA will continue production support and maintenance of PAID during the Department's migration to the new payroll provider, DFAS, and the eHR Line of Business providers and systems. As a result of continued operations, accreditation and the authority to operate the PAID system must be maintained. Efforts are currently underway to complete the activities needed to maintain this status.

e-Payroll Accomplishments and Plans

VA continues to make system changes needed to support VA's migration to DFAS. System



changes were tested internally and externally by completing payroll cycles in both VA and DFAS and comparing results. The first group of VA employees was successfully migrated to DFAS in 2006. The second group, which included additional Title 5 employees, migrated in October 2007. Planning for the migration of the remaining 230,000 VA employees is underway. VA and DFAS are continuing to complete additional system changes to support the migration initiative. The remaining VA payroll facilities will begin migration in 2008 with the last migration occurring tentatively in February 2009.

In 2008 work will continue on completing the planning, analysis, and development of system changes required for the National Institutes of Health's (NIH) time and attendance system which interfaces with DFAS. The NIH system will be implemented in VA, using a phased approach.

E-Gov Travel Accomplishments and Plans

The FSC, VA's E-Government Travel Service (ETS) Project Office, is leading VA's implementation of ETS as well as supporting VA's legacy travel systems. In the first quarter of 2007, VA travelers comprising 45 percent of VA's temporary duty travel volume migrated to ETS using the FedTraveler Web-based application. This migration allowed VA to close down the Zegato legacy travel system. During the third quarter of 2007, VA conducted a pilot with the first group of non-Zegato travel system users. The pilot began the rollout of 21 "Go Live" events that will end with VA fully migrated to the FedTraveler application by December 2007. As the implementation of FedTraveler.com continues with weekly station deployments, the FSC has focused on training, communication, and support as the key strategy for a successful implementation. One of the key performance measurements the General Services Administration (GSA) monitors is the online adoption rate, which measures the percentage of travel plans with air reservations made using the online booking engine. VA's online adoption

rate through the fourth quarter of 2007 averaged 81 percent, above VA's 75 percent goal, and leads all of the Electronic Data System's government deployments.

Other Systems Accomplishments and Plans

Electronic Commerce (EC)/Electronic Data Interchange (EDI). Using COTS software and national standards, the FSC moves mission-critical information between VA and each of its trading partners, which includes vendors, mortgage service providers, and health care entities. EC/EDI also provides for internal exchange of information among VA application systems. Electronic data transfers enable program offices to restructure their work processes, take advantage of the accuracy and timeliness of electronic data, and concentrate on service objectives. The FSC will continue to support VA's efforts to increase cost savings and program efficiencies through the expansion of electronic data transfers in VA applications.

In addition to providing EC/EDI to VHA, the FSC provides these services to VA's Denver Acquisition and Logistics Center for invoices and payment vouchers. Commercial invoices, Financial Management System payments, and the subsistence prime vendor program services are also provided to VA nationwide. VBA benefits from EC services in FSC's accepting and processing status of loan default transactions. EDI services are also provided by the FSC to assist the Veterans Canteen Service in receiving and processing invoices and purchase orders as well as creating payment transactions.

The FSC continues to provide support to the U.S. Department of Agriculture (USDA). Under a franchise agreement, the FSC accepts invoices from USDA Utility and Telecommunications providers, translates them to a USDA-approved file format, and transfers these invoices to USDA via a secure connection. USDA inputs these invoices into its legacy systems for processing and payment. This processing takes place using FSC-owned translator software



rather than the mainframe translator, which ensures license compliancy and reduces processing costs for USDA.

The FSC will continue to support VA's efforts to increase cost savings and program efficiencies through the expansion of electronic data transfers in VA applications. The FSC will also continue to support VHA's efforts to comply with EC/EDI mandates identified in the Health Insurance Portability and Accountability Act (HIPAA) of 1996 and improve VHA's revenue

cycle. The FSC continues to use the latest versions of software to electronically ensure the validity of data with regard to HIPAA electronic transaction requirements.

In our efforts to provide VHA with e-Claims reports, the FSC has created a portal for management reports. This portal allows managers to access up-to-date statistics of their data. The portal will be updated to include new reports as requested.

Electronic Commerce (EC)/Electronic Data Interchange (EDI) Planned Improvement Initiatives

Tasks	Target Dates
Migrate customers to server-based translation software.	2008-2009
Support MCCR lockbox receipt of payments.	2008-2012
Support (by providing both development and production support services) VHA's revenue cycle and HIPAA compliance efforts.	2008-2012
Support EDI production projects on a continuing basis.	2008-2012
Support reports portal.	2008-2012

On Line Certification System (OLCS) (payment certification). The FSC's OLCS application, an *e-GOV 2000 Trailblazer* award winner, allows certifying officials to view and certify invoices electronically. Vendors send invoices directly to the FSC where they are scanned into the FSC's document management optical imaging system and electronically stored with the information required to process the invoice. Field stations can elect to certify all invoices via OLCS or allow automatic payment for those invoices under \$2,500 with appropriate post-payment audits. For invoices to be certified online, the OLCS system sends an e-mail notification to certifying officials with information on how to access and certify the pending invoice(s) online. Over 10,000 employees currently use the OLCS within VA.

OLCS was an essential enabler in centralizing VHA certified invoice payment processing to the FSC. Certified invoices sent to the FSC for processing are managed by certifying officials

through the OLCS and paid by the FSC. As a result, VA has realized a tremendous increase in the efficiency of the payment process. At the same time, the OLCS and centralization have substantially reduced interest penalties and increased discounts earned.

The FSC's certified payments process represents a full life cycle of services performed from receipt of the invoice until the Department of the Treasury (Treasury) renders payment. The services include processing cancelled checks, check tracers, vendor re-certifications, rejects and adjustments, inquiries, vendor reclaims, bills of collection, Treasury offsets, and tax levies that comply with applicable VA regulations and directives and the Prompt Payment Act.

Document Management System (DMS). The FSC uses a document imaging system, referred to as DMS, to provide a paperless work environment, reduce physical storage needs, and process high volumes of documents. Documents



are stored on electronic media, with backups stored offsite, and can be retrieved in seconds.

Initially, DMS was used to process commercial payments and inquiries. Subsequently, the FSC's use of DMS has been expanded to include other functions such as vendorizing requests, federal accounts, preparation of the Standard

Form-224 report, storing grant and schedule documents for other government agency customers, storing payroll folder data for VA employees who receive local payroll services from the FSC's OLCS, and the storage of fee basis medical claims.

Planned DMS Expansion and Support

Tasks	Target Dates
Provide program support for DMS.	FY 2008-FY 2012