



STATEMENT OF DAVID M. ZAVADA

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U.S. DEPARTMENT OF HOMELAND SECURITY

BEFORE THE

COMMITTEE ON GOVERNMENT REFORM

SUBCOMMITTEE ON
GOVERNMENT MANAGEMENT, FINANCE AND ACCOUNTABILITY

U.S. HOUSE OF REPRESENTATIVES

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Mr. Chairman Platts, Ranking Member Towns, and Members of the Subcommittee.

I am David M. Zavada, Assistant Inspector General for Audits of the Office of Inspector General (OIG) at the Department of Homeland Security (DHS). Thank you for the opportunity to discuss the status of financial management at DHS, efforts to address the Department's internal control weaknesses, and implementation of the *Department of Homeland Security Financial Accountability Act*, P.L. 108-330 (Accountability Act).

Office of Inspector General Partnerships

The Office of Inspector General partners with the Secretary of Homeland Security and Congress to ensure that the Department accomplishes its mission in the most effective, efficient, and economical manner. Key to achieving these objectives is sound financial management. Through our audits, we provide independent, objective information and identify issues and opportunities for improvements in financial management and other areas.

We share with the Chief Financial Officer (CFO) a vision of world-class financial management that delivers reliable, timely, and useful information to support the critical mission of DHS. Financial management is a high-priority area for our office - - it is an area where we plan an ongoing and proactive presence. Our goal is to provide the Department with real-time analysis and feedback to assist them as they are developing and executing financial improvement plans.

The DHS Financial Accountability Act and Internal Control

Strong financial management and accountability are essential to effectively and efficiently accomplish DHS's mission. The Accountability Act recognizes this and emphasizes effective financial management leadership and internal control as essential elements of a sound financial management program. This Act made DHS subject to the *Chief Financial Officers Act of 1990*, P.L. 101-576, similar to other large departments and agencies. As a result, the Department now has a Senate-confirmed CFO with a statutorily established direct reporting relationship to the Secretary and clearly defined responsibilities.

The Accountability Act also emphasizes the importance of good internal control as a foundation for timely and reliable financial information. To this end, the Accountability Act has very specific requirements with respect to internal control over financial reporting by requiring the Secretary to include in the Department of Homeland Security (DHS) *Performance and Accountability Report* (PAR) an assertion on internal control over financial reporting. DHS met this requirement in 2005 with the Secretary asserting that the Department was unable to provide reasonable assurance that internal control over financial reporting was effective.

The Act further requires the Secretary to include an audit opinion on the Department's internal control over financial reporting in DHS's PAR, beginning in FY 2006. The Department will meet this requirement, with our office providing this opinion.

In addition, to further promote internal control improvements, we have undertaken a series of performance audits focusing on the Department's corrective action plans to address internal control weaknesses. Performance audits assess the effectiveness and efficiency of program management and initiatives. The intent of these audits is to assess the Department's progress in preparing well-developed corrective action plans to support internal control improvements. Our corrective action plan audits are being conducted on a real-time basis by providing recommendations to strengthen plans as they are being developed. I will discuss the results of these audits later in this statement.

Status of Financial Management at DHS

Creating a Financial Management Capacity

Financial management has been a major challenge for DHS since its creation in 2003. DHS was created by consolidating 22 domestic agencies, many of these agencies brought to DHS different business processes and pre-existing internal control weaknesses. In addition, DHS needed to create a Department-level capacity to lead, manage, and oversee financial management. We have reported in our financial audit report that this has proven to be a challenging task for the Department. Specifically, in our past audits we have identified resource and capability deficiencies in Department-level financial management oversight and reporting.

2005 Financial Audit Results

For FY 2005, financial management within the Department continued to falter. The Department was again unable to receive an opinion on its financial statements and ten material internal control weaknesses were reported for the second straight year. KPMG, LLP, under contract with the OIG, issued a disclaimer of opinion primarily due to problems at Immigration and Customs Enforcement (ICE) and the Coast Guard. However, the Office of Financial Management (OFM), within the OCFO, Transportation Security Administration (TSA), State and Local Government Coordination and Preparedness (SLGC&P), and Emergency, Preparedness and Response (EP&R) also experienced difficulties they could not overcome by the reporting deadline, and joined ICE and the Coast Guard in contributing to the Department's overall disclaimer of opinion. Those difficulties included: a systems conversion at TSA, problems involving timely access to information from SLGCP's accounting service provider, and Hurricane Katrina, which stretched EP&R's accounting resources late in the fiscal year.

The Department's ten material internal control weaknesses ranged from financial management oversight and reporting at the department-level to controls surrounding the recording of individual account balances within DHS bureaus. The material weaknesses are pervasive throughout the Department and are indicative of the challenges the Department faces in producing timely and reliable financial information.

Many of these weaknesses are attributable to significant internal control problems at ICE, Coast Guard and the OCFO. These control weaknesses, due to their materiality, are impediments to obtaining a clean opinion and positive assurance over internal control at the department level.

FY 2006 Activities

To move forward, DHS must develop a comprehensive financial management strategy that addresses organizational resources and capabilities, inconsistent and flawed business processes, and unreliable financial systems. An initial step in this process is to prepare well-developed and comprehensive corrective action plans to address known internal control weaknesses.

During FY 2006, we anticipated progress in addressing internal control deficiencies. The Department identified four areas where internal control weaknesses exist for improvement during the year. However, a coordinated Department-wide effort to develop corrective action plans did not begin until the third quarter of 2006; and as of the completion of our recent performance audits, the Department did not yet have a Department-wide plan in place.

Many of the Department's material weaknesses, to varying degrees, are attributable to the Coast Guard. Achieving a clean financial statement audit opinion and providing positive assurance over internal control at the Department level is highly dependent upon internal control improvements at the Coast Guard.

The Coast Guard does not yet have well-developed corrective action plans to address their internal control weaknesses. For example, a milestone of their plan to address weaknesses in financial management oversight and structure is to form a transformation team to develop a plan - - this amounts to a plan to develop a plan. The Coast Guard also has not yet undertaken a through analysis of its business processes and financial systems to determine the root causes of its many internal control weaknesses.

Also, ICE began its component corrective action plan process early, during the first quarter of 2006, and should show signs of internal control improvements this year. It is also evident that senior financial management leadership within the Department are actively engaged in developing an overall financial management strategy, corrective action plans and in developing systems to monitor overall internal control improvement efforts.

However, these steps alone will not be sufficient to turn the corner for FY 2006. Weaknesses within the OCFO rooted in resources and capabilities continue to exist along with the work of remediation of most other weaknesses. Given these weaknesses and the lack of progress in addressing them, producing a PAR, including consolidated financial statements, on an accelerated schedule, remains a considerable challenge. Existing internal control weaknesses at the OCFO, Coast Guard, and ICE remain the primary reasons.

Performance Audits of Department Corrective Action Plans

Over the past several months we initiated a series of performance audits to assess the effectiveness of DHS's corrective action plans to address internal control weaknesses. Our objective in conducting these performance audits is to assess the thoroughness and completeness of both the overall corrective action plan process and individual plans developed to address specific weaknesses. The performance audits are intended to provide ongoing feedback to the Department as they are developing and implementing corrective action plans.

Our performance audit analysis and related recommendations focus on four essential elements of good corrective action plans. These areas are: identification of "root cause" problems, development of critical milestones, accountability for accomplishing corrective actions and validation that actions taken were effective. We also looked for linkage between critical milestones in the plans with overall goals, and for integration of the corrective action plan process with other related management activities; the most significant of which is implementation of the internal control assessment requirements in OMB Circular A-123, *Management's Responsibility for Internal Control*. To date, we have completed two audits focused on assessing the overall corrective action plan process and specific corrective action plans for four of the ten material weaknesses the Department prioritized for improvement in 2006.

Performance Audit Report No. 1: The Overall Corrective Action Plan Process

During 2006, DHS initiated a formal corrective action plan effort aimed at developing corrective action plans and tracking specific milestones for its material internal control weaknesses. As part of this effort, the Department developed a detailed automated tracking system to monitor corrective action plan progress. Our first performance audit focused on assessing the process and guidance the Department has put in place and the overall progress in developing a Department-wide corrective action plan.

We recommended that the Department enhance its process and guidance by:

- further emphasizing management's responsibility for internal control and move away from a disproportionate reliance on external audits;
- providing additional tools for analyzing the "root cause" of internal control deficiencies;
- better integrating corrective action plans with other related management assessment and corrective action plan initiatives; and
- establishing clearer accountability for completing corrective actions.

To date, much of the Department's identification of internal control deficiencies has been through the financial statement audit. While our financial audit will continue to report on internal controls, we recommend that greater responsibility be taken by the Department for assessing and correcting internal control deficiencies. As the Department develops these processes further, we recommend that they be closely integrated and leveraged with

the OMB Circular A-123 assessment process. We also recommended greater coordination with corrective action plans being developed and implemented to address information technology weaknesses. Similarly, roles and responsibilities of responsible officials and accountability need to be clear and coordinated.

Our audit also reported that the Department did not begin a coordinated corrective action plan effort until the third quarter of FY 2006. Although DHS now has a formal corrective action plan process in place and has begun to implement this process within DHS components, it has not yet prepared an overall Department-wide corrective action plan.

Performance Audit Report No. 2 - - Assessing Corrective Action Plans for 2006 Department Priority Areas

Our second performance audit focused on assessing the Department's progress in developing specific corrective action plans for four internal control weaknesses it prioritized for improvement in FY 2006. These weaknesses are:

- financial management oversight,
- financial reporting,
- accounting for Fund Balance with Treasury, and
- accounting for Actuarial Liabilities.

These weaknesses are primarily attributable to three entities within the Department: the OCFO, ICE, and Coast Guard.

In auditing the Department's corrective action plan efforts in these four areas, we assessed specific corrective action plans developed to address these weaknesses within the above three entities. Consistent with our approach in performance audit number one, we looked for all the elements of well-developed corrective action plans.

Overall we identified well-developed corrective action plans at ICE and some progress at the OCFO. We reported very little progress in developing effective corrective action plans at the Coast Guard. Our audit report provides recommendations for improvement for all three entities.

Office of the Chief Financial Officer

Weaknesses related to financial management oversight and financial reporting relate primarily to resource and capability issues within the OCFO. We have reported a need for increased OCFO oversight and financial reporting capabilities since FY 2004. Proper resourcing at the OCFO is critical to improving financial management within the Department. The OCFO has developed corrective action plans for material weaknesses related to its financial management oversight and financial reporting, but the plans need further development.

During FY 2006, the OCFO demonstrated some progress in initiating a Department-wide corrective action plan process and taking steps to actively monitor progress. As part of its corrective action plan process related to financial management oversight, management has identified the need for a comprehensive organizational, staffing, and human resource needs study to carry out its responsibilities in this area. We recommended that management conduct its planned study as a basis for developing a more robust corrective action plan to address its oversight responsibilities.

Corrective action plans related to financial reporting contained routine financial management task rather than specific actions to address underlying problems. To address financial reporting weaknesses the OCFO has hired a contractor to enhance its financial reporting capability. To achieve lasting improvements in this area corrective actions need to be better developed. We recommended that further analysis of “root causes” be performed and detailed corrective action tasks with time sensitive milestones be developed, assigned for completion and validated.

Immigration and Customs Enforcement

ICE proactively began its corrective action plan process in the first quarter of FY 2006. Consequently, they are further along in developing and executing corrective action plans than the other DHS entities. ICE created a Program Management Office (PMO) to develop and implement a three-year Financial Action Plan. The PMO reports directly to the ICE CFO and provides program management infrastructure, guidance and support to staff developing and implementing corrective action plans. We found corrective action plans to be comprehensive and well developed. In addition, ICE senior leadership has set a positive tone for financial management improvements and actively monitors progress.

For FY 2006, ICE prioritized implementation of its plans, with a goal of fully remediating its Fund Balance with Treasury material weakness. The 2006 financial statement audit underway will assess the effectiveness of ICE’s implementation of its plan.

To improve further their corrective action plans, we recommended that ICE better define the criteria used to determine when a corrective action is complete and integrate the validation process with control testing planned for conducting management’s OMB Circular A-123 assessment.

Coast Guard

The Coast Guard developed corrective action plans intended to address weaknesses in each of the four priority areas. We reported that these plans were general in nature and lacked adequate detail. Underlying root causes were limited to only those previously identified through the financial statement audit. Consequently, the corrective action plans did not include a fully developed and detailed listing of tasks to correct weaknesses, a timeframe for completion or adequate accountability.

We made specific recommendations related to all key elements of the Coast Guard’s plans. Our primary recommendations are for the Coast Guard to improve its corrective

action plans by performing a thorough root cause analysis of weaknesses that includes a review of financial systems, processes and human resources and develop a detailed list of tasks and milestones based upon this analysis. We also recommended the Coast Guard make a realistic assessment of the resources required to plan and execute corrective actions. Further, in filling key financial management vacancies, ensure that the position holders have the necessary skills to execute corrective action plans and seek sustained support for the plan from executive leadership.

Other Corrective Action Plan Performance Audits

We are currently working to complete our third performance audit of corrective action plans. This performance audit is targeted at the Department's efforts to address six material weaknesses in the areas of Property, Plant and Equipment; Operating Materials and Supplies; Undelivered Orders; Accounts and Grants Payable; Disbursements; Budgetary Accounting; and Intragovernmental and Intradepartmental Balances. The OCFO, Coast Guard, ICE, TSA, and Office of Grants and Training have drafted corrective action plans intended to address their respective contribution to these material weaknesses. For our fourth audit, we plan to focus in greater depth on further plans being developed by the Coast Guard to transform and improve overall financial management. We look forward to briefing this Committee on both of these reviews in the future.

Conclusion

We intend to continue taking a proactive and engaged approach to overseeing DHS' financial management improvement efforts through our financial statement audits and performance audits covering DHS's financial systems, corrective action plans, and the implementation of OMB Circular A-123. We look forward to conducting these audits and providing the results to the Secretary and the Congress.

Mr. Chairman, this concludes my prepared remarks. I would be happy to answer any questions that you or the Committee Members might have.

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