

DEPARTMENT OF HOMELAND SECURITY Office of Inspector General

Audit of DHS' Corrective Action Plan Process for Financial Reporting – Report No. 1



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**Homeland
Security**

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Preface

The Department of Homeland Security (DHS) Office of Inspector General (OIG) was established by the Homeland Security Act of 2002 (*Public Law 107-296*) by amendment to the Inspector General Act of 1978. This is one of a series of audit, inspection, and special reports published by our office as part of our oversight responsibility to promote economy, efficiency, and effectiveness within the department.

This report is the first of a series of OIG performance audit reports intended to provide an assessment of planned DHS corrective actions to improve internal control. Improving internal control is a critical objective of the DHS Financial Accountability Act (*Public Law 108-330*). The report is based on interviews with employees and officials of relevant agencies and institutions, direct observations, and a review of applicable documents. We contracted with the independent public accounting firm KPMG LLP to perform the audit. KPMG is responsible for the attached auditor's report and the conclusions expressed in it.

The recommendations herein have been discussed in draft with those responsible for implementation. It is our hope that this report will result in more effective, efficient, and economical operations. We express our appreciation to all of those who contributed to the preparation of this report.

A handwritten signature in cursive script that reads "Richard L. Skinner".

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KPMG is pleased to submit this performance audit report related to the Department of Homeland Security's overall corrective action plan process in fiscal year 2006. The Department of Homeland Security Office of Inspector General engaged us to perform a series of performance audits for fiscal year 2006 and to meet the objectives identified in the Background, Objectives, and Scope section of this report.

We conducted our first performance audit from May 1, 2006 through May 31, 2006, in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. The purpose of this report is to communicate the results of our performance audit and the related findings and recommendations, which are discussed in detail in the Findings and Recommendations section of this report. Management prepared a response which is presented at the end of this report and concurred with our recommendations.

Since May 31, 2006, we have not performed any additional procedures with respect to this performance audit and have no obligation to update this report or to revise the information contained therein to reflect events occurring subsequent to May 31, 2006.

KPMG LLP

Executive Summary

Overall, the Department of Homeland Security (Department) is working on adopting a corrective action methodology that is structurally sound. However, challenges continue to exist in developing an effective department-wide corrective action plan (CAP) and in effectively implementing and overseeing planned corrective actions.

Findings and Recommendations

All findings and recommendations are classified by either relating them to the overall CAP process or one of the following four broad phases generally found in an effective CAP process: (1) Identification of the underlying root cause, (2) Development of an effective remediation plan, (3) Accountability for establishment and successful implementation of the CAP, and (4) Validation of the successful implementation of the CAP.

Process and Guidance

The Department has initiated a CAP process which has established policies and procedures in the financial management arena. The DHS Management Directive (MD) 1030, *Corrective Action Plans*, and *DHS Corrective Action Plan (CAP) Process Guide Version 1* (CAP Guide) are first steps towards the Department's incremental progress in developing a sustainable financial management architecture that will provide users with reliable financial information.

KPMG has identified several conditions for management's consideration to improve the Department's guidance and tools, as follows:

Overall

- A. Development of a Department-wide CAP***
- B. Integration of the CAP Process with Other Departmental Activities***

Identification

- C. Establishment of Management's Responsibility for Identifying Internal Control Deficiencies***
- D. Determination of Cause and Documentation of Results***

Development

- E. Establishment of Timeframes***

Validation

- F. Development of Verification and Validation Procedures***
- G. Development of Performance Measures and Milestones***

Technology

We believe that the Department's use of the Electronic Program Management Office (ePMO) application represents an improvement over the previous manual CAP monitoring process. Although the implementation of ePMO will be an ongoing process, indicators suggest that this application can be an effective tool for assisting the Department in monitoring findings and their

related CAPs. However, we identified the following opportunity for improvement related to technology:

Overall

H. Establishment of Training

Resources

The Department does not have the proper accountability infrastructure necessary for the effective implementation of a CAP process for fiscal year 2006 (FY2006), nor are the lines of communication explicitly and specifically laid out in the CAP Guide.

KPMG identified the following opportunity for improvement related to the Department's resources and accountability infrastructure:

Accountability

I. Development of Accountability Infrastructure

Background, Objectives, and Scope

Background

Office of Management and Budget (OMB) Circular A-123, *Management's Responsibility for Internal Control*, states "Federal agencies are subject to numerous legislative and regulatory requirements that promote and support effective internal control. Effective internal control is a key factor in achieving agency missions and program results through improved accountability. Identifying control weaknesses and taking related corrective actions are critically important to creating and maintaining a strong internal control infrastructure that supports the achievement of agency objectives."

OMB Circular A-123 builds upon the internal control framework within the *Standards for Internal Control in the Federal Government* (Green Book), issued by the Government Accountability Office (GAO), which defines internal control as an "integral component of an organization's management that provides reasonable assurance that the objectives of (a) effectiveness and efficiency of operation, (b) reliability of financial reporting, and (c) compliance with applicable laws and regulations are being achieved."

To meet the objectives above, management is responsible for developing and implementing internal control activities, as outlined in the Green Book, that comply with the following standards for internal controls:

- Control Environment – the organizational structure and culture created by management and employees to sustain organizational support for effective internal control.
- Risk Assessment – the identification of internal and external risks that may prevent the organization from meeting its objectives.
- Control Activities – the policies, procedures and mechanisms in place to help ensure that agency objectives are met.
- Information and Communication – the communication of relevant, reliable, and timely information to relevant personnel at all levels within an organization.
- Monitoring – the periodic review, reconciliation, or comparison of data included as part of the regular assigned duties of personnel, as well as the periodic assessment of the effectiveness of internal control. Deficiencies identified whether through internal review or by an external audit should be evaluated and corrected. A systemic process should be in place for addressing deficiencies.

As stipulated in OMB Circular A-123, management's process for designing corrective action plans to address the Department's ten identified material weaknesses in internal control must:

- "Provide for appointment of an overall Corrective Action Accountability Official from senior agency management. The corrective action accountability official should report to the Department's Senior Management Council, if applicable.
- Require prompt resolution and corrective actions.
- Maintain accurate records of the status of identified material weaknesses through the entire process of resolution and corrective action.
- Assure the corrective action plans are consistent with laws, regulations, and Administration policy.
- Assure that performance appraisals of appropriate officials reflect effectiveness in resolving or implementing corrective action for identified material weaknesses."

The Department has undertaken several initiatives in the area of internal control in FY2006. One initiative, which is the focus of this performance audit, is the development and implementation of a formal corrective action plan process. Under this initiative, the Department issued (a) Management Directive (MD) 1030, *Corrective Action Plans*, on May 15, 2006, (b) the *DHS Corrective Action Plan (CAP) Process Guide* (CAP Guide), dated April 28, 2006, and (c) the *Corrective Action Plan Quick Reference* card (CAP Card); deployed the use of a web-based software application, Electronic Program Management Office (ePMO), to manage the collection and reporting of CAP information for the Department and its components; and held a training course on April 28, 2006, for Department and component level employees which focused on the MD 1030, the CAP Guide, the CAP Card, and ePMO. Under this initiative, the Department's intent is to position itself to move forward in its objective of obtaining an unqualified audit opinion on its consolidated financial statements, as well as on its internal controls over financial reporting.

The purpose of MD 1030 is to establish the "Department's vision and direction on the roles and responsibilities for developing, maintaining, reporting, and monitoring CAPs specific to the *DHS Financial Accountability Act*, *Federal Managers' Financial Integrity Act (FMFIA)*, and related OMB guidance." In addition to the roles and responsibilities, MD 1030 outlines the policies and procedures related to the CAP process. The organizational structure detailed in MD 1030 encompasses employees at both the component and department levels.

The purpose of the CAP Guide is to "outline the policies and procedures for developing, maintaining, reporting and monitoring CAPs throughout the Department, as well as assisting employees with CAP responsibilities in their understanding of the CAP process, the types of required data, and the level of detail necessary to meet DHS and OMB requirements." The CAP Guide explicitly states that it was "developed exclusively for internal control over financial reporting (ICOFR) and applies to all DHS components and Departmental Offices where a control deficiency has been identified, except for non-conformances related to the *Federal Information Security Management Act (FISMA)*." FISMA related non-conformances are under the purview of the Department's Chief Information Security Officer's *Plan of Action and Milestones (POA&M) Process Guide*.

The CAP Card indicates that the CAP process consists of three steps: (1) Identify Internal Control Deficiency, (2) Conduct Root Cause Analysis, and (3) Corrective Action Plan. Step 3 includes information on the general CAP process cycle and is taken verbatim from the CAP Guide.

Objectives

The purpose of this performance audit was to report on the Department's overall CAP process as of May 31, 2006. Our audit was conducted in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States; specifically, the standards for performance audits.

The objective of this performance audit was to report on the status and evaluate the effectiveness of the Department's overall plan to (1) develop well-written and meaningful CAPs, which include milestones, specific actionable steps to address the Department's ten material weaknesses, and identification of sufficient resources to develop and monitor the CAPs, and (2) ensure adherence by the components to milestones and progress.

Scope

The scope of this performance audit was the Department's CAP process for FY2006 as of May 31, 2006, with a focus on the process and guidance, technology, and resources. The Department is in

the early stages of its CAP process, and accordingly, management has represented that its approach and supporting documents will be frequently updated and improved during the process. Our audit was limited to a review of the CAP Guide which is only one document of many to be produced by the Department. For example, our scope did not include an audit of or procedures on any specific CAP related to the Department's ten material weaknesses cited in the independent auditors' report on the Department's consolidated financial statements as of and for the year ended September 30, 2005, included in the Department's *Performance and Accountability Report, Fiscal Year 2005*.

The timeline for this performance audit was as follows:

- Fieldwork/Reporting – May 1, 2006 through May 31, 2006
- Draft Report – June 1, 2006
- Final Report – June 15, 2006

Performance Audit Approach

We performed a variety of performance audit procedures over the CAP Guide, which was the only documentation available for review at the time of our audit, and certain limited aspects of the CAP process. Our methodology consisted of the following four-phased approach:

Phase I – Project Initiation and Planning

To initiate and focus the performance audit approach, we conducted kick-off meetings with the Department's OIG and OCFO. These meetings included a review of the objectives and the scope of the project, as well as collaboration among the participants (i.e. KPMG, OIG, and OCFO). In addition, during the meetings with the OIG, criteria deemed to be reasonable, attainable, and relevant to the performance audit objectives were identified for Phase III of the audit (see Phase III below for further information).

Phase II - Assessment of Process and Related Guidance

- ***Department OCFO Interviews***

We interviewed the select OCFO personnel having CAP process responsibilities to gain a detailed understanding of the CAP process. These interviews focused on policies and procedures (i.e., guidance) issued by the OCFO, technology tools (e.g., ePMO) provided by the OCFO to be utilized during the CAP process, the OCFO's overall goals for the process, roles and responsibilities, the current process implementation results and planned future action steps.

- ***CAP Process Training Seminar***

We attended an OCFO-administered training seminar on the CAP Guide and ePMO. This training provided information on the CAP Guide, roles and responsibilities, process implementation deadlines, and ePMO. In addition, the training highlighted the results of the Coast Guard's "pilot" implementation of ePMO.

- ***CAP Policies and Procedures and Technology Tools***

- We read MD 1030 to determine the roles and responsibilities defined by the OCFO to govern the development, maintenance, reporting, and monitoring of CAPs (i.e., the CAP process).

- We reviewed the CAP Guide and the CAP Card to gain an understanding of the policies and procedures established to develop, maintain, report, and monitor CAPs.
- In addition, we gained an understanding of the technology tools provided by the OCFO to implement the CAP process. Specifically, we received training from the Department on ePMO's functionality and reviewed the CAP Guide, which provides illustrations on how ePMO can support the CAP process.

The interviews with select OCFO personnel having CAP process responsibilities, attendance at the Department's CAP training seminar, inspection of CAP policies and procedures, and training received on technology tools used to support CAP policies and procedures helped us to form our understanding of the CAP process and assess its current "as-is" state.

Phase III - Gap Analysis

We reviewed existing project management and internal control monitoring practices and guidance for "leading" practices that could serve as our evaluation criteria. We then compared our understanding of the Department's existing CAP process to the "leading" practices to identify gaps. These gaps reflect situations that could negatively impact the implementation of the Department's CAP process if corrective action is not taken.

The existing project management and internal control monitoring practices and guidance we reviewed included:

- The GAO *Standards for Internal Control in the Federal Government* (Green Book) as the underlying framework in evaluating the overall CAP process;
- Internal methodology regarding project management and internal control evaluation;
- CAP guides published by other Federal agencies;
- OMB Executive Branch Management Scorecard; and
- OMB Circular A-123.

We categorized the gaps into three areas:

- Process and Guidance – How effectively and efficiently the CAP process is conducted, including policies and procedures;
- Technology – How technology tools are used to enable the CAP process; and
- Resources – How resources are organized, available, and utilized.

Phase IV - Recommendations

After conducting our gap analysis in Phase III, we formulated a recommendation for each gap identified.

Findings and Recommendations

Effective CAP processes generally contain four broad phases:

- Identification of the underlying root cause is an important phase in the CAP process. Accurate identification of the root cause mitigates the chances of recurrence. Many times symptoms of

the deficiency are identified rather than the root cause. By identifying only the symptoms, it is difficult to develop an effective CAP that will successfully resolve the deficiency.

- Development of an effective remediation plan is the appropriate way to cure an internal control deficiency. A key component of an effective plan is the inclusion of both attainable and measurable milestones to allow both the Department and the component effectively monitor the remediation process.
- Accountability is vital to the CAP process because it necessitates the establishment of an individual CAP owner who is responsible for its successful implementation. The owner's responsibilities include ensuring that milestones are achieved and that the validation phase is completed.
- Validation is important in order to verify that the CAP has been successfully completed. It should include activities that will provide evidence to support the closure of the CAP. These activities should include documentation reviews, work observations, and performance testing.

All findings and recommendations are classified by either relating them to the overall CAP process or one of the four phases discussed above.

Process and Guidance

We identified the following findings or gaps with respect to the Department's CAP process. We recognize that the Department is at the early stages of implementing this process. Most of these findings are related to the CAP Guide, which was issued April 28, 2006. The Department anticipates issuing additional versions of the CAP Guide to address any "gaps" identified and incorporate lessons learned. These findings are further classified by either relating to the overall CAP process or to one of the four phases discussed above.

Overall

A. Development of a Department-wide CAP

Conditions

One of the Department's financial reporting objectives in FY2006 is to reduce the number of material weaknesses in internal control. The CAP Guide, dated April 28, 2006, was issued almost seven months into FY2006. While separate corrective actions were underway in certain Department components preceding the release of the CAP Guide, the Department did not launch its coordinated, centralized, Department-wide approach to development and implementation of CAPs until the 3rd quarter. Earlier in the fiscal year, the OCFO was focused on completing the Department's FY2005 financial statement audit, then on developing a CAP process including the procurement of contractor assistance. As a result, the Department has had little time to fully implement the corrective actions to affect the FY2006 financial statement audit. Under the new guidance, the Department did not require submission of component CAPs until the end of May 2006, and accordingly as of the date of this report, has not been able to review and accept the component CAPs.

We noted, however, that the Department worked closely with the components to meet its first milestone date of May 31, 2006, whereby all components were required to update their current CAPs into the new format, as stated in the CAP Guide, for input into ePMO by the Department. It is likely that the Department's review will result in some adjustments to the component CAPs, requiring time for revisions and iterative dialogue between the Department and components. As a result, the Department may not have fully approved CAPs until sometime in the 4th quarter of fiscal 2006, or in FY2007. Because of the lack of fully approved individual CAPs, the development of a

consolidated, Department-wide CAP prioritizing Department-wide objectives has not occurred. As a result, management lacks the ability to link corrective actions with the affected financial statement line items.

Recommendations

1. We recommend that DHS review its remediation objectives to ensure goals are realistic and achievable. Realistic timelines will allow for thoroughness and quality remediation.
2. We recommend the Department develop a consolidated, Department-wide CAP that prioritizes and brings into focus Department-wide objectives. This Department-wide CAP will also facilitate a linkage between the corrective actions and the affected financial statement line items, providing management with a timeline of when assertions such as accuracy and completeness of the financial statements can be made to leadership, in the PAR, and to the auditors.

B. Integration of the CAP Process with Other Departmental Activities

Conditions

The Department's CAP Guide has not been integrated with the Department's Chief Information Security Officer's *Plan of Action and Milestones (POA&M) Process Guide*, the Department's *Performance and Accountability Report (PAR) Guide*, nor the implementation of OMB Circular A-123. The Department tracks its CAPs (intended for financial reporting control deficiencies) separately from POA&Ms (intended for FISMA related non-compliance). The CAP Guide does not discuss how corrective processes for deficiencies that might overlap with both financial reporting and FISMA should be coordinated, or who is responsible for completing this task. In addition, the CAP Guide does not include guidance on how to address and integrate the corrective processes for control deficiencies identified by other external reviews, e.g., GAO High Risk Series and OIG Top Management Challenges, in the Secretary's Assurance Statements issued in accordance with FMFIA. OCFO personnel told us that they are working towards including these other areas in future releases of the CAP Guide. The lack of integration of the various manuals and/or activities may result in redundancies in operations and/or the ineffective utilization of the Department's limited resources.

Recommendations

3. We recommend that the Department structure its corrective action activities so that guidance is integrated and ensures that all deficiencies are properly prioritized, and effectively and efficiently addressed. This will require coordination between the CFO and CIO. Enhancements are needed so that the CAP Guide, the POA&M Process Guide and the PAR Guide work together, instead of independently.
4. We recommend that the Department compare the initial bureau and, once developed, the overall CAPs to the Department's implementation plan for OMB Circular A-123, to ensure that both processes are coordinated and executed in unison. The Department's implementation plan should include guidance on the extent and frequency of procedures required to follow-up on corrective actions, once implemented, to ensure they have been designed appropriately, are operating effectively, and, if necessary, timely modifications are made.

Identification

C. Establishment of Management's Responsibility for Identifying Internal Control Deficiencies

Conditions

- a) The CAP Guide does not emphasize that management is primarily responsible for identifying control deficiencies. The guidance for identifying control deficiencies, as written, is not well

balanced between input from the financial statement audit process, and perhaps more importantly, management's self assessment which is being conducted as part of the implementation of OMB Circular A-123. OMB Circular A-123 states that process analysis must occur to assess the adequacy of the process for identifying and managing risks. Risk points should be identified, categorized by potential impact if the risk was unmitigated, and brought to the attention of the risk owners so that they may acknowledge the risk and accept responsibility.

As OMB Circular A-123 process analyses are performed, management will gain a greater understanding of the internal control activities in place and where gaps exist. Additionally, there is institutional knowledge resident with the employees of the Department and the components that could be used to expand the database of potential control deficiencies. For example, we noted that a component has coined the phrase "known conditions" for areas of improvement that have been identified internally versus those identified by the external auditor.

It is not apparent that all components understand that they must take ownership for the success of their business processes and not rely on the external auditor to identify control deficiencies.

- b) The CAP Guide does not clearly describe the importance of separating management's own assessment of the control deficiency, and the resulting CAP, from the external auditors' recommendations. The external auditors' recommendations are based on knowledge gained while performing an audit, the objective of which is not to give an opinion on internal controls. The auditor makes no assertion that implementing its recommendation(s) will fully remediate the conditions, or that all of the related control conditions have been identified and reported in their independent auditors' report. Accordingly, the auditor can not assure management that implementation of a recommendation will completely remove the deficiency until the condition is tested during the next audit cycle. Therefore, Department management has responsibility for identifying and implementing all remediation steps.
- c) Section 3.1 of the CAP Guide, "Identify Control Deficiencies and Reach Consensus," provides the process to follow when resolving disagreements between the external auditor and management. Although establishing a process for handling disagreements is appropriate, this should take place separate from a CAP. Management's acceptance or disagreement with an audit finding is inherent in the financial statement audit process and must occur prior to the development of a CAP. Management's agreement with, and intent to correct, a control deficiency is the starting point for a CAP.

Recommendations

- 5. We recommend that the CAP Guide be revised to emphasize management's responsibility for identifying control deficiencies and emphasize the importance of using management's judgment to identify control deficiencies by closely integrating their OMB Circular A-123 assessment and corrective action processes. The Department should perform its own walkthroughs and testing procedures over its controls to determine if they are designed and operating effectively. These procedures should be outlined in the Department's OMB Circular A-123 guide and referenced in the CAP Guide. Other resources, such as the external auditor, should be used as a supplement to management's judgment, not in its place.
- 6. We recommend that other Department components consider using the approach adopted by the component referred to above and identify and track known conditions where financial reporting risks exist.
- 7. We recommend that the Department clearly distinguish the CAP process from external auditor dispute resolution protocols. The beginning of the CAP process should be management's identification of, and intent to resolve, a control deficiency.

D. Determination of Cause and Documentation of Results

Conditions

- a) Section 3.4 of the CAP Guide states the importance of understanding the root cause of a deficiency before development of the CAP. However, the CAP Guide does not provide guidance on how to gain this understanding (e.g., tools to use or possible questions to ask, etc.). The root cause analysis is an essential component to the development of a CAP, and could, by itself, become a project, especially when the weakness is caused by structural and systemic problems. The CAP Guide recognizes the need for a root cause analysis but does not provide further guidance often found in other Federal Departments' CAP guidance that we reviewed.

One Federal agency's CAP guidance that we reviewed provided considerations to be used when evaluating a deficiency, how to gather information, how to identify "causal factors" (i.e., the root cause), and how to develop corrective actions. Another Federal agency's CAP guidance included examples of questions that were used in determination of the root cause such as:

- Is the Department policy/procedure clear?
- Have employees been adequately trained to perform the process?
- Does the policy address who performs the process, how, and when?

This particular guide further discusses the importance of continuing to ask "why" until the evaluator extends beyond the symptoms of the deficiency and arrives at the actual root cause.

- b) Additionally, the CAP Guide does not include guidance on how to document the results of determining the cause of the deficiency. Without proper documentation, there is no evidence for a reviewer to confirm that the appropriate root cause of the deficiency was in fact identified. For example, we noted that another Federal agency's CAP guidance specifically states that information collected during this process relating to the deficiency should be documented and used in development of the CAP.
- c) The OCFO has devised an innovative approach to deal with the difficult subject of root cause analysis. They have instituted bi-weekly "root cause workshops" where members of the OCFO meet to discuss and brainstorm deficiencies and the root causes. This is an important first step in bringing together people for the sole purpose of asking the question "why." Presently, the root cause workshops are only held by the OCFO and the Department's CAP Guide does not discuss these workshops and their role in the CAP process.

Recommendations

8. We recommend that the Department amend the CAP Guide to provide further guidance to components on how to identify the underlying cause of a deficiency. The general steps to conducting this analysis should be included in the CAP Guide to provide the user with a starting point. The general process should include identifying the problem, collecting data, analyzing the cause/effect relationship, and finally identifying the root cause. The guidance also should include useful methodology, tools, and examples of how a detailed analysis should be performed to differentiate symptoms from root causes.
9. We recommend that the Department require its components to thoroughly document the root cause analysis performed and conclusions reached. The documentation should be retained for review by independent auditors, if necessary. Documentation of this process is important to serve as evidence for the reviewer. A standard template could be developed for performing this analysis to ensure that the responsible party is addressing the appropriate issues. Implementation of this recommendation should be performed in close coordination with the

Department's OMB Circular A-123 assessment, due to the significant over-lap of review and documentation requirements.

10. We recommend that the Department facilitate "root cause workshops" at all components to increase the effectiveness of the CAP process since components are typically in a better position to answer the question "why."

Development

E. Establishment of Timeframes

Condition

The CAP Guide does not give any general guidance on the timeframe for each significant element of the CAP process, e.g., identification, development, accountability, and validation. Section 4.10 of the CAP Guide includes guidance on the scheduled due dates of the corrective action plan. This section states that due dates should be determined based on realistic estimates. This guidance appears to offer flexibility to components to properly plan and implement corrective actions without unreasonable pressures that could result in diminished quality, and also establishes that management expects the timeframes to be "realistic." However, the CAP Guide could be improved by (1) providing timeframe guidance on each significant element of the CAP process, and (2) generally setting out management expectations in terms of broad goals and objectives.

As a benchmark, we noted that another Federal agency's CAP guidance states that "all material weaknesses and noncompliance issues must be corrected within one year." This guidance further states that "to ensure deficiencies are corrected prior to the beginning of the next year's audit process, final correction of the deficiency should end on June 30, to allow sufficient time for testing. All extensions are to be granted by management."

Recommendation

11. We recommend that the CAP Guide be enhanced by (1) providing timeframe guidance on each significant element of the CAP process, e.g., identification, development, accountability, and validation, and (2) generally setting out management expectations in terms of broad goals and objectives. Timeframes should consider prioritization of corrective actions, resource needs and appropriate funding. Management must strive for a proper balance between its objective to reduce or eliminate control deficiencies and obtain an unqualified audit opinion on its consolidated financial statements, as well as on its internal controls over financial reporting, and providing components with sufficient time to make effective improvements.

Validation

F. Development of Verification and Validation Procedures

Condition

The CAP Guide does not describe the methodology that should be used by the components for verification and validation of control deficiencies. Section 4.6 of the CAP Guide includes guidance on verification and validation of control deficiency milestones to determine if deficiencies have been corrected, and whether the control objectives meet the requirements of OMB Circular A-123, Appendix A. It states that testing procedures should be documented and properly supported by evidence. However, the CAP Guide lacks a description of the methodology, e.g., individuals to be involved with the reviews, techniques used to validate the findings, and development of corrective actions. For example, the CAP Guide does not require components to consider segregation of duties in the development and validation of corrective actions, which could lead to biased points of view, and eventually to the implementation of less than optimal solutions. We noted that another Federal agency's CAP guidance included guidance on developing effective review plans, who should be

involved, different types of review activities, validation of the effectiveness of corrective actions, reporting, and follow up procedures.

Recommendation

12. We recommend that the Department include a detailed methodology in its CAP Guide to ensure that the verification and validation stage of the process results in an effective approach that not only corrects the control deficiency, but also integrates and supports other financial reporting and management initiatives of both the component and the Department. The verification and validation process should be closely integrated as part of the OMB Circular A-123 internal control assessment process. Some areas of this section of the CAP Guide should be expanded to provide further guidance on documentation requirements, performance testing, acceptable testing procedures, analysis of results, and who needs to be involved in the process.

G. Development of Performance Measures and Milestones

Conditions

- a) The CAP Guide requires the user to establish key performance measures and milestones, however, the guidance does not link the two, or indicate how often in the CAP process the measurements should be performed, or even what the measurements should generally achieve. Section 4.4 of the CAP Guide includes guidance on establishing key performance measures to monitor the effectiveness of corrective actions. This section states that these performance measures should be objective, measurable, and quantifiable. Section 4.8 of the CAP Guide includes guidance on establishing milestones to track the progress of corrective actions. The user of the CAP Guide is allowed to create measurements and milestones that they believe are appropriate, which may not provide the Department with the information needed, in a timely manner, to monitor progress and prepare external reports, e.g., OMB.
- b) The CAP Guide does not include guidance on the extent or frequency of procedures required to follow-up on corrective actions, once implemented, to ensure they have been designed appropriately and are operating effectively. Section 3.7 of the CAP Guide includes guidance on continuously monitoring and updating CAP activities based on events that occur. We noted that another Federal agency's CAP guidance required the performance of follow-up procedures, including "performing internal control assessments on a pre-determined basis (e.g., quarterly), and/or continuous monitoring of metrics previously established during the corrective action planning process."

Recommendations

13. We recommend that the CAP Guide be amended to provide more specific guidance on what key performance measures and milestones should be used, and how often during the CAP process the measurements should be performed. Specifically, the CAP Guide should indicate that key performance measures and milestones be performed during both the CAP implementation process, as well as the post-implementation monitoring phases in an effort to facilitate the tracking of follow-up procedures. Continuous monitoring and updating of CAP activity is not only important while the CAP is still in process, but is also an important element of ensuring that the deficiency does not recur once the CAP has been completed.
14. We recommend that the Department consider linking performance measures to established milestones as a means of measuring the progress over certain time periods. The performance measures and milestones can then be consolidated by the Department into a comprehensive Gantt chart and used for internal and external reporting of both achieved and planned progress.
15. We also recommend that the Department compile a summary-level report measuring CAP progress against specific metrics and milestone criteria. Such a report could be modeled after

the OMB's Executive Management Scorecard to provide a user-friendly performance summary at a glance.

Technology

With the implementation of the Department's CAP process, the Department deployed ePMO, a web-based software application to manage the collection and reporting of CAP information for the Department and its components. ePMO has several features to allow the components and the Department to monitor CAP progress. Such features include (a) a search function which conducts a database-wide search and returns relevant records and file attachments that contain the search word, (b) multiple view options for CAPS (e.g., by due date, by status, and by person), and (c) various reports (e.g., CAP Summary Report and CAP Detailed Report).

The CAP Guide stipulates that all information in the CAP be updated and accurate on the last day of the month, although the components are encouraged to use ePMO as a monitoring tool and to update it on a continuous basis as events occur.

Overall

H. Establishment of Training

Condition

Users of ePMO were not required to attend training that was offered by the Department on the functionality of the application. Since training was optional, to date, several components' designated users have not received training on ePMO. Consequently, the Department has launched a software application and required its use by component employees who may not have adequate knowledge to fully and properly comply with the Department's reporting and monitoring directive. This could lead to delayed or even erroneous information being reported by the components, which could then lead to inaccurate reporting internally to Department executives and externally to other interested parties, e.g., OMB. With the deployment of any new application, users must fully understand the functionality and capability of the application. As such, training of the users is essential. It is our understanding that the Department was willing to provide training to each component's designated users of ePMO. Although the Department contacted each component to schedule such training, not all components were scheduled for training if the component indicated that it did not consider training of its users necessary. Training, however, is essential to the correct and effective use of the system.

Recommendation

16. We recommend that the Department implement a policy requiring all users of ePMO at each component to receive mandatory training offered by the Department prior to granting the user access rights to ePMO.

Resources

The Department identified a group of professionals, identified as the Financial Accountability and Controls Branch, led by a Manager within the OCFO, which is responsible for implementation of the CAP process. Analysts within this branch support the Financial Reporting Branch's efforts to ensure quality financial reporting data, maintain ePMO, and monitor the components' CAP progress. The Department has also engaged several outside contractors to assist in the implementation of the CAP process. The primary contractor was responsible for assisting the OCFO in the development of the CAP Guide as well as assisting with Department-wide training.

Accountability

I. Development of Accountability Infrastructure

Condition

The MD 1030 and/or the CAP Guide create several unique roles and responsibilities for financial executives and personnel throughout the Department though it is unclear how these roles and responsibilities will be aligned with other financial management initiatives of the Department, e.g., FISMA, performance measures, and OMB Circular A-123. For example, new positions and committees such as the DHS Senior Management Council (SMC), Corrective Action Accountability Officials (CAAO's), and Responsible Party (RP's) have been created. While it is early in the CAP process, we noted some positions named by the CAP Guide have not been filled, and that some positions do not have "position descriptions" that more clearly define how, what and when responsibilities are to be performed. For example, it is not clear to whom the Audit Follow-up Official reports. Therefore, it is unclear whether the persons designated to fill the positions have the proper background, experience, capability and time to perform the work. It is also unclear at this early stage of the CAP process how the various roles will interact with one another to successfully implement change at both the component and the Department level.

Secondly, the Financial Accountability and Controls Branch, a branch within the OCFO whose sole responsibility is to promote the implementation and continuance of sound internal control throughout the OCFO's financial reporting process, is not mentioned in either the MD 1030 or the CAP Guide.

Finally, the MD 1030 and the CAP Guide do not explicitly state the accountability hierarchy to ensure quantifiable progress is sustained during the execution of the CAP process. The only specific reference in the MD 1030 and the CAP Guide is under the responsibilities of the CAAO where it states that they are responsible for assuring that performance appraisals of appropriate officials reflect effectiveness in resolving or implementing corrective action for identified material weaknesses, reportable conditions, and non-conformance.

Recommendations

17. We recommend that the Department enhance the CAP Guide by further defining roles and responsibilities in the next version. This will help the components better understand their role, management's expectations, definition of success in performance and milestone measurements, and help ensure that the CAP process is executed in a timely and coordinated manner.
18. We recommend the Department create an organizational chart that clearly establishes the lines of communication and authority of the various positions and committees. This should be formally documented so that no misunderstanding of roles and responsibilities occurs.
19. We recommend that the Department hold all active participants in the CAP process accountable through the use of the performance appraisal process. In order to do this, the Department should institute fair and accurate reporting as a true measure of the progress being made and use this reporting to evaluate management's performance.


U.S. Department of Homeland
Security
Washington, DC 20528



Homeland Security

June 22, 2006

MEMORANDUM FOR: Richard L. Skinner, Inspector General

FROM: David L. Norquist, Chief Financial Officer 

SUBJECT: Audit of DHS' Corrective Action Plan Process for Financial Reporting – Report No. 1

Thank you for the opportunity to comment upon the Audit of DHS' Corrective Action Plan Process for Financial Reporting – Report No. 1. I am pleased to report that we concur with the 19 recommendations. We will ensure our developing corrective action planning process addresses the issues raised in the report. Highlights of significant actions currently underway include the following:

- Development of an *Internal Control Over Financial Reporting (ICOFR) Playbook* to establish a unified DHS corrective action plan (CAP) to guide our efforts over FY 2007 and 2008;
- Execution of process level assessments across the Department to serve as a formal “root-cause” analysis to build stronger corrective action plans;
- Planning and collaboration with the Department’s Chief Information Security Officer to conduct pilots for integration of the FISMA and OMB A-123 assessment processes; and
- Scheduling of CAP workshops to train DHS Components on the new ePMO system and CAP Guide.

I appreciate the balanced tone of the report and acknowledgement of our efforts. In closing, we look forward to continue our partnership in implementing corrective actions and most importantly the DHS Financial Accountability Act.

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