



Department of Homeland Security Office of Inspector General

Independent Auditor's Report on
DHS' FY 2009 Special-Purpose Financial Statements





**Homeland
Security**


NOV 16 2009

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 prepared as part of our oversight responsibilities to promote economy, efficiency, and effectiveness within the department.

This report presents the independent auditor's report on DHS' FY 2009 special-purpose financial statements. We contracted with the independent public accounting firm KPMG LLP (KPMG) to perform the audit. KPMG is responsible for the attached report dated November 16, 2009, and the conclusions expressed in it. We do not express opinions on DHS' financial statements or internal control or provide conclusion on compliance with laws and regulations.

We trust 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


for Richard L. Skinner
Inspector General



KPMG LLP
2001 M Street, NW
Washington, DC 20036

INDEPENDENT AUDITORS' REPORT

Secretary and Inspector General
U.S. Department of Homeland Security:

We were engaged to audit the accompanying Closing Package Financial Statement Report-Balance Sheet of the Department of Homeland Security (DHS or Department) as of September 30, 2009 and 2008, and the accompanying Financial Report (FR) Notes Reports (except for the information in the FR Notes Reports entitled "threshold") for the years then ended; the accompanying Additional Note Nos. 29 and 30; and the accompanying Trading Partner Summary Note Report – Balance Sheet as of September 30, 2009 and 2008 (hereinafter collectively referred to as the special-purpose financial statements). These special-purpose financial statements are the responsibility of DHS management.

We were not engaged to audit the related accompanying Closing Package Financial Statement Reports - Statement of Net Cost and Statement of Changes in Net Position for the years ended September 30, 2009 and 2008, and the related Trading Partner Summary Note Reports-Statement of Net Cost and Statement of Net Position for the years ended September 30, 2009 and 2008 (hereinafter referred to as "other fiscal year 2009 and 2008 Closing Package Financial Statement Reports").

The accompanying special-purpose financial statements have been prepared for the purpose of complying with the requirements of Chapter 4700 of the U.S. Department of the Treasury's *Treasury Financial Manual* (TFM), as described in Additional Note Nos. 29 and 30, solely for the purpose of providing financial information to the U.S. Department of the Treasury and the U.S. Government Accountability Office (GAO) to use in preparing and auditing the *Financial Report of the U.S. Government*, and are not intended to be a complete presentation of DHS' balance sheets as of September 30, 2009 and 2008.

In accordance with *TFM Chapter 4700*, DHS prepared FR Notes Report Nos. 2 through 28B, except for FR Notes Report Nos. IOA, 21, 23, and 24, which were not applicable to DHS. DHS included Additional Note Nos. 29 and 30 to disclose data not contained in the special-purpose financial statements, but which is necessary to make the special-purpose financial statements more informative.

The United States Coast Guard (Coast Guard) was unable to provide sufficient evidential matter that support transactions and certain balance sheet accounts including fund balance with Treasury, accounts receivable, inventory and related property, general property, plant and equipment including heritage assets and stewardship land, actuarially-derived liabilities, environmental and other liabilities, and net position, as reported in the accompanying DHS special-purpose financial statements as of September 30, 2009 and 2008. The total assets of the Coast Guard, as reported in the accompanying DHS special-purpose financial statements were \$18.8 billion and \$17.4 billion, or 22 and 20 percent of total DHS consolidated assets as of September 30, 2009 and 2008, respectively.

The Transportation Security Administration (TSA) was unable to provide sufficient evidential matter that supports certain general property, plant, and equipment balances and related effects on net position, as reported in the accompanying DHS special-purpose financial statements as of September 30, 2009 and 2008. The TSA general property, plant, and equipment balances reported in the accompanying DHS special-purpose financial statements were \$997 million and \$932 million as of September 30, 2009 and 2008, respectively, or 6 percent of DHS' consolidated general property, plant, and equipment in both years.

In addition, we were unable to obtain certain representations from DHS management regarding the matters described above, including representations as to compliance with U.S. generally accepted accounting principles, with respect to the accompanying DHS special-purpose financial statements as of September 30, 2009 and 2008, and were unable to determine the effect of the lack of such representations on the FY 2009 and 2008 DHS special-purpose financial statements.

Because of the matters discussed in the three preceding paragraphs, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the accompanying special-purpose financial statements of DHS as of September 30, 2009 and 2008. However, we noted the following discrepancies in FR Notes Report – Note 22 Earmarked Funds – Section F- Revenue, Financing, Expenses, and Other - Prior Year:

Line Number	Line Description	Column Headings	As Reported	Correct Amount
21	Customs User Fees	Other taxes and receipts	\$435m	\$1,925m
		Intragovernmental transfers, net	\$-0-	\$(1,490)m
26	All other earmarked funds	Other taxes and receipts	\$2,347m	\$857m
		Intragovernmental transfers, net	\$(1,405)m	\$85m

We were not engaged to audit the accompanying other fiscal year 2009 and 2008 Closing Package Financial Statement Reports and, accordingly, we do not express an opinion on them.

As discussed in FR Notes Report No. 17, DHS restated its fiscal year 2008 financial statements to correct multiple errors identified by TSA, Coast Guard, United States Customs and Border Protection, United States Immigration and Customs Enforcement, National Protection and Programs Directorate (NPPD), United States Citizenship and Immigration Services, Federal Law Enforcement Training Center, and the Science and Technology Directorate that required adjustment of balances previously reported in DHS' fiscal year 2008 financial statements.

DHS also prepared Other Data Report Nos. 1 through 16, except for Other Data Report Nos. 3 through 8, and 11 through 14, which were not applicable to DHS. The information included in Other Data Report Nos. 1, 2, 9 (except for the information in the section entitled "Threshold"), 10, and 15 is presented for the purpose of additional analysis and is not a required part of the special-purpose financial statements, but is supplementary information required by U.S. generally accepted accounting principles and the *TFM Chapter 4700*. We were unable to complete limited procedures over this required supplementary information, as prescribed by professional standards, because of the limitations on the scope of our audits described above. Certain information in the Other Data Report Nos. 1 and 16 is based on other fiscal year 2009 and 2008 Closing Package Financial Statement Reports which we were not engaged to audit. This information has not been subjected to the auditing procedures, and accordingly, we express no opinion on it.

The information in Other Data Report No. 16; the information entitled "Threshold" in Other Data Report No.9; the information entitled "Threshold" in FR Notes Report Nos. 2, 5, 6, 11, 12, 14, 15, and 19; the information in the Closing Package Line Reclassification Summary Report-Balance Sheet; the information in the Closing Package Line Reclassification Summary Reports - Statements of Net Cost and Changes in Net Position; and the information in Closing Package Line Reclassification Summary Report – Custodial Activity is presented for purposes of additional analysis and is not a required part of the special-purpose financial statements. This information has not been subjected to the auditing procedures applied in the audits of the special-purpose financial statements and, accordingly, we express no opinion on it.

The *TFM Chapter 4700* requires agencies to use the Government-wide Financial Reporting System to input certain data as described in Additional Note No. 29. We express no opinion on information maintained in that system.

In accordance with *Government Auditing Standards* and OMB Bulletin No. 07-04, *Audit Requirements for Federal Financial Statements*, we have also issued a combined report, dated November 13,2009, which discusses the reasons why we were unable to express an opinion on DRS' balance sheets as of September 30,2009 and 2008, and on the related statements of custodial activity for the years then ended; why we were unable to express an opinion on internal control over financial reporting of the DRS balance sheet as of September 30,2009, and statement of custodial activity for the year then ended; and the results of our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, and other matters that are required to be reported under *Government Auditing Standards*. That report is an integral part of our engagement to audit DRS' balance sheets as of September 30, 2009 and 2008, and the related of custodial activity for the years then ended, and should be read in conjunction with this report in considering the results of our engagement to audit the special-purpose financial statements. Our engagement to examine the Department's internal control over financial reporting of the DRS balance sheet as of September 30, 2009, and statement of custodial activity for the year then ended disclosed material weaknesses, significant deficiencies, and compliance and other matters, as follows:

Material weaknesses in internal control over financial reporting have been identified in the following areas:

- Financial Management and Reporting
- Information Technology Controls and Financial System Ftilctionality
- Fund Balance with Treasury
- Property, Plant, and Equipment and Operating Materials and Supplies
- Actuarial and Other Liabilities
- Budgetary Accounting

Significant deficiencies have been identified in the following areas:

- Other Entity Level Controls
- Custodial Revenue and Drawback

Non-compliance with laws, regulations, contracts, and grant agreements have been identified in the following areas:

- *Federal Managers' Financial Integrity Act of 1982*, and laws and regulations supporting OMB Circular No. A-50, *Audit Follow-up*, as revised
- *Federal Financial Management Improvement Act of 1996*
- *Single Audit Act Amendments of 1996*

- *Chief Financial Officers Act of 1990*
- *Anti-deficiency Act*

The following other matters have been identified:

We also reported other matters related to compliance with the *Anti-deficiency Act* at NPPD, Federal Emergency Management Agency, United States Secret Service, and Coast Guard.

As discussed in our *Independent Auditors' Report* dated November 13, 2009, the scope of our work was not sufficient to express an opinion on DRS' balance sheets as of September 30, 2009 and 2008 or statements of custodial activity for the years then ended. In addition, the Coast Guard was unable to provide documentation of key processes, risk assessments, or evidence supporting the existence of internal controls, and management acknowledges that pervasive material weaknesses exist in key financial processes, and was therefore unable to make an assertion on the effectiveness of internal control over financial reporting. Accordingly, we were unable to perform the examination procedures necessary to form an opinion on DRS' internal control over financial reporting of the balance sheet as of September 30, 2009, and statement of custodial activity for the year then ended.

Other deficiencies in internal control, potentially including additional material weaknesses and significant deficiencies, and other instances of non-compliance may have been identified and reported had we been able to perform all procedures necessary to express an opinion on DRS' balance sheets as of September 30, 2009 and 2008, and the related statements of custodial activity for the years then ended, and had we been engaged to audit the related statements of net cost, changes in net position, and budgetary resources, for the years then ended; and had we been able to perform all procedures necessary to express an opinion on DRS' internal control over financial reporting of DRS' balance sheet as of September 30, 2009, and statement of custodial activity for the year then ended, and had we been engaged to examine internal controls over financial reporting of the other related FY 2009 financial statements.

Management is responsible for establishing and maintaining internal control. In planning and performing our engagement to audit the fiscal year 2009 special-purpose financial statements we also considered DRS' internal control over financial reporting by obtaining an understanding of DRS' internal control over financial reporting of the special-purpose financial statements as a basis for designing our audit procedures, but not for the purpose of expressing an opinion on the effectiveness of DRS' internal control over financial reporting of the special-purpose financial statements. Accordingly, we do not express an opinion on the effectiveness of DRS' internal control over financial reporting of the special-purpose financial statements.

Our consideration of internal control over financial reporting for special-purpose financial statements was for the limited purpose described in the preceding paragraph of this section and would not necessarily identify all deficiencies in the internal control over financial reporting for special-purpose financial statements that might be significant deficiencies or material weaknesses.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

In our fiscal year 2009 engagement to audit the special-purpose financial statements, we did not identify any additional deficiencies in internal control over financial reporting of the special-purpose financial statements that we consider to be material weaknesses as defined above. However, had we been able to perform all of the procedures necessary to express an opinion on the special-purpose financial statements, other matters involving internal control over financial reporting and compliance with *TFM Chapter 4700* requirements relating to the special purpose financial statement may have been identified and reported.

Management is responsible for complying with laws, regulations (including *TFM Chapter 4700*), contracts, and grant agreements applicable to DHS. As part of our engagement to audit DHS' fiscal year 2009 special-purpose financial statements, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of special-purpose financial statement amounts. However, providing an opinion on compliance with those provisions or on compliance with *TFM Chapter 4700* requirements was not an objective of our fiscal year 2009 engagement to audit the special-purpose financial statements and, accordingly, we do not express such an opinion.

The results of our tests of compliance with *TFM Chapter 4700* disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 07-04. However, had we been able to perform all of the procedures necessary to express an opinion on the special-purpose financial statements, other matters involving compliance with certain provisions of laws, regulations, contracts, and grant agreements and compliance with *TFM Chapter 4700* requirements relating to the special-purpose financial statements may have been identified and reported.

This report is intended solely for the information and use of DHS management, the DHS Office of Inspector General, U.S. Department of Treasury, OMB, and GAO, in connection with the preparation and audit of the *Financial Report of the U.S. Government*, and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

November 16, 2009

Report Distribution

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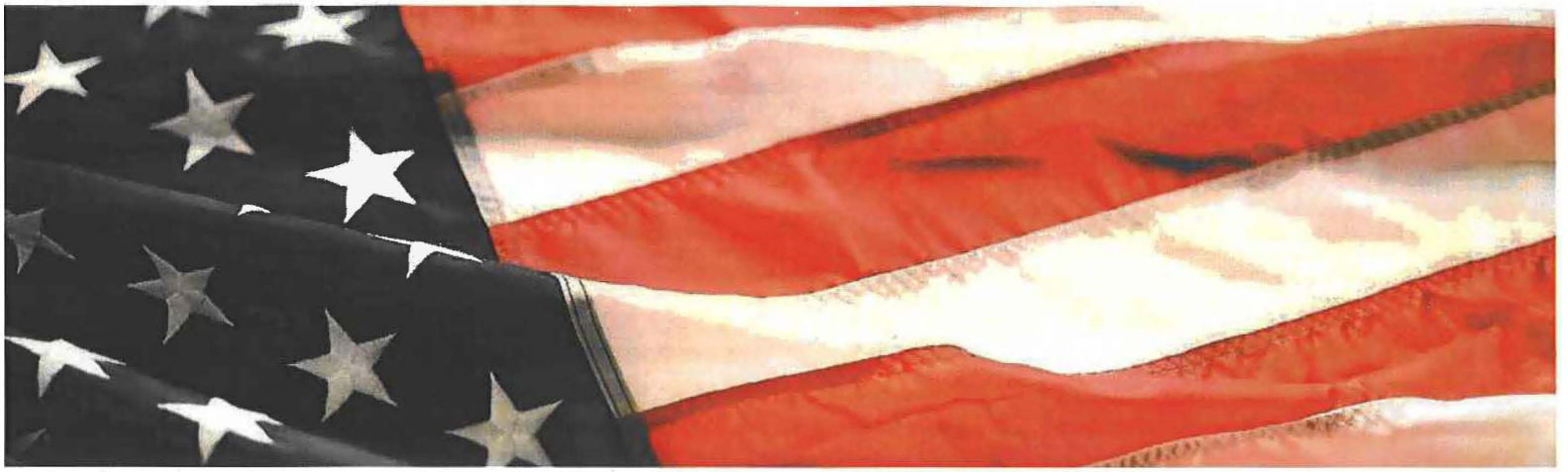
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