

Department of Homeland Security Office of Inspector General

Department of Homeland Security's
Compliance with the Improper Payments
Elimination and Recovery Act of 2010





Homeland
Security

MAR 13 2012

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 addresses the strengths and weaknesses of the Department's process to estimate and report improper payments as well as its efforts to reduce and recover improper payments. It is based on interviews with employees and officials of relevant agencies and institutions, direct observations, and a review of applicable documents.

The recommendations herein have been developed to the best knowledge available to our office, and have been discussed in draft with those responsible for implementation. 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.

A black and white image of a handwritten signature, which appears to read "Anne L. Richards".

Anne L. Richards

Assistant Inspector General for Audits

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Abbreviations

AFR	Annual Financial Report
CBP	U.S. Customs and Border Protection
DHS	Department of Homeland Security
DNDO	Domestic Nuclear Detection Office
FEMA	Federal Emergency Management Agency
FY	fiscal year
GAO	Government Accountability Office
ICE	U.S. Immigration and Customs Enforcement
ICRM	Internal Control and Risk Management
IPERA	<i>Improper Payments Elimination and Recovery Act of 2010</i>
IPIA	<i>Improper Payment Information Act of 2002</i>
KPMG	KPMG LLP
MAPS	mission action plans
NPPD	National Protection & Programs Directorate
OCFO	Office of the Chief Financial Officer
OIG	Office of Inspector General
OMB	Office of Management and Budget
USCG	U.S. Coast Guard
USSS	U.S. Secret Service
S&T	Science and Technology Directorate
TSA	Transportation Security Administration

OIG

*Department of Homeland Security
Office of Inspector General*

Executive Summary

Federal government agencies reported an estimated \$125 billion in improper payments in fiscal year 2010. Congress passed the *Improper Payments Elimination and Recovery Act of 2010* in an effort to reduce these erroneous payments. The Act requires each agency's Inspector General to annually determine if the agency is in compliance with the Act.

Our audit objectives were to 1) determine if the Department of Homeland Security is in compliance with the Act; 2) evaluate the accuracy and completeness of the Department's improper payment reporting; and 3) evaluate the Department's efforts in reducing and recovering improper payments for fiscal year 2011.

We contracted with KPMG LLP to determine whether the Department of Homeland Security complied with the Act. KPMG LLP did not find any instances of noncompliance with the Act.

We reviewed the accuracy and completeness of the Department's improper payment reporting and its efforts to reduce and recover improper payments. The Department needs to 1) improve controls to ensure completeness and accuracy of reporting and 2) increase efforts to recover improper payments. Specifically, the Department should ensure that all payments subject to testing are tested and reported and that recovery audit rates are reported accurately. Independent parties should perform test work and review sample payments. Also, the Department should develop guidance on applying results of test work using alternative sampling methodologies. Finally, the Department should perform recovery audits when cost effective, and those audits should target payments with a higher potential for overpayment and recovery.

We made six recommendations that if implemented would improve the accuracy and completeness of the Department's improper payment reporting and improve its efforts to recover any overpayments. DHS concurred with all six of our recommendations.

Background

The federal government's efforts to reduce improper payments predate the Department of Homeland Security (DHS). In 2002, the Government Accountability Office (GAO) reported, based on estimates voluntarily provided by some agencies, that the federal government made approximately \$20 billion in improper payments annually for fiscal years (FYs) 1999, 2000, and 2001. GAO believed the actual figure could be much higher because no authority required agencies to comprehensively measure, report, and reduce improper payments, and few agencies had publicly reported improper payment information.

In response, Congress passed the *Improper Payments Information Act of 2002* (IPIA). IPIA required the head of each agency to annually review all their programs and activities, identify the programs susceptible to significant improper payments, and report estimated improper payments for programs identified as susceptible. For programs with estimated improper payments exceeding \$10 million, IPIA required agencies to report the causes of the improper payments, actions taken to correct the causes, and the results of the actions taken.

On July 22, 2010, the President signed the *Improper Payments Elimination and Recovery Act* (IPERA or the Act). IPERA amended IPIA by expanding requirements for identifying, estimating, and reporting on programs susceptible to significant improper payments. The term improper payment:

- A. means any payment that should not have been made or was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements; and
- B. includes any payment to an ineligible recipient, any payment for an ineligible good or service, any duplicate payment, any payment for a good or service not received (except where such payment is authorized by law), and any payment that does not account for credit for applicable discounts.¹

Improper payments in a program or activity become "significant" if, in the preceding fiscal year, improper payments exceeded: (a) \$10 million and 2.5 percent of total program outlays or (b) \$100

¹ Pub. L. 111-204, Section 2.(e).

million regardless of the improper payment percentage of total program outlays.²

IPERA requires agencies to perform risk assessments on all programs and activities. Agencies must then test programs and activities susceptible to significant improper payments, and annually report the estimated improper payments made, the actions taken to reduce improper payments, and efforts to recover overpayments.³

In FY 2011, DHS reported an improper payment estimate of \$210 million from 14 programs across six Components:

Table 1: DHS' FY 2011 Estimated Improper Payment Amounts and Rates

<u>DHS Component</u>	<u>Programs Tested</u>	<u>Payment Population (\$ millions)</u>	<u>Estimated Improper Payments (\$ millions)</u>	<u>Improper Payment Rate (%)*</u>
U.S. Customs and Border Protection	2	\$1,449	\$3	0.21%
Federal Emergency Management Agency	8	\$3,720	\$68	1.83%
U.S. Immigration and Customs Enforcement	1	\$1,332	\$108	8.12%
National Protection and Programs Directorate	1	\$811	\$27	3.27%
Transportation Security Administration	1	\$2,458	\$0	0.01%
U.S. Coast Guard	1	\$2,918	\$4	0.13%
DHS-wide	14	\$12,688	\$210	1.66%

Source: DHS-OIG analysis using data from DHS FY 2011 *Annual Financial Report* (AFR). DHS calculated its FY 2011 estimated improper payment rates using FY 2010 payment data. *Improper payment percentages are weighted averages where multiple programs were reported.

² Pub. L. 111-204, Section 2.(a).

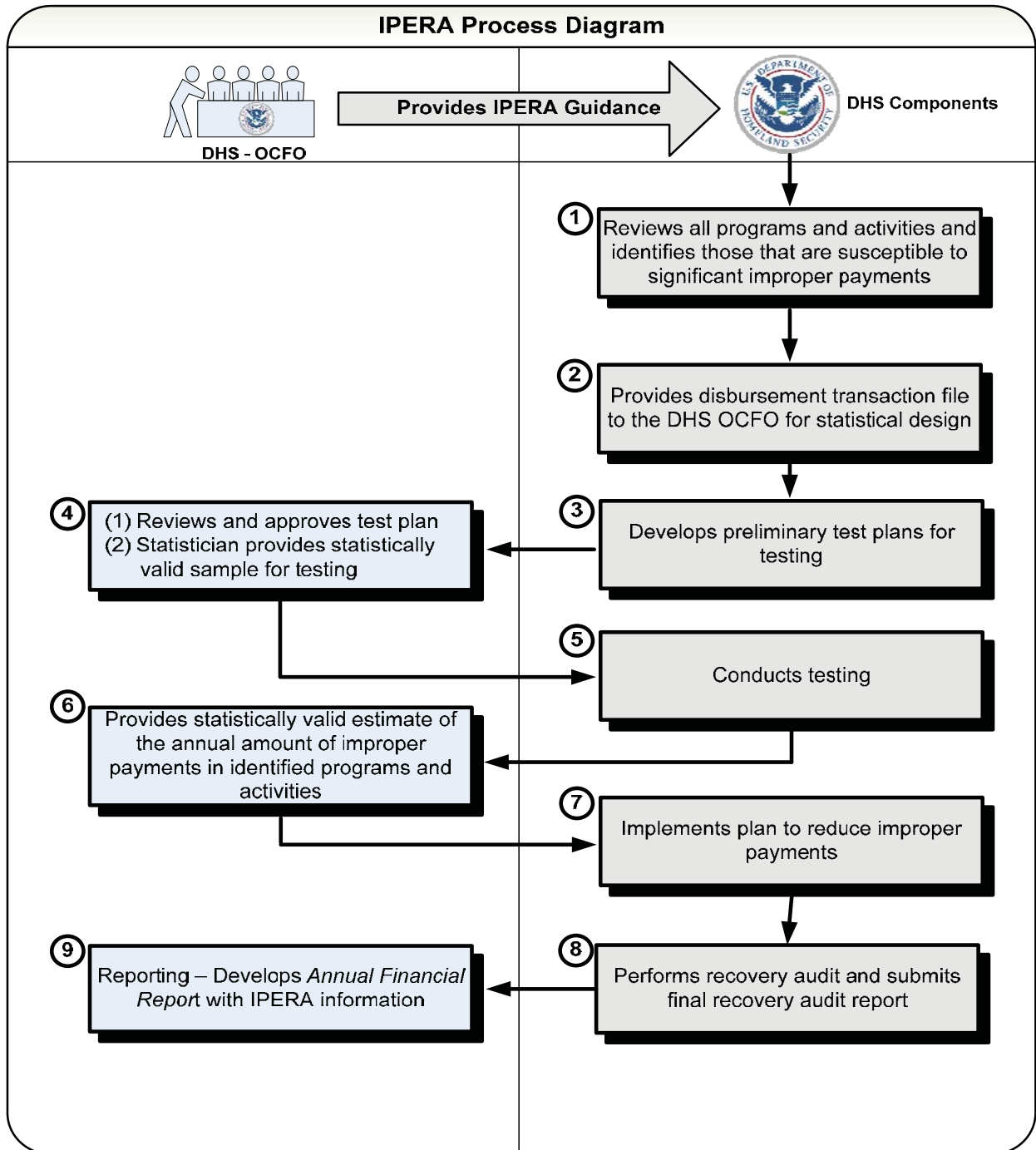
³ Pub.L.111-204, Section 2.(a), (b),and (d).

We reviewed the processes and procedures for DHS and the following DHS Components:

- U.S. Coast Guard (USCG);
- U.S. Customs and Border Protection (CBP);
- Federal Emergency Management Agency (FEMA);
- U.S. Immigration and Customs Enforcement (ICE);
- National Protection and Programs Directorate (NPPD);
- Science and Technology Directorate (S&T); and
- Transportation Security Administration (TSA).

In November 2010, the DHS Internal Control Program Management Office issued version 1.0 of its *Improper Payments Reduction Guidebook*. This *Guidebook* provides DHS Components with instructions for complying with IPERA, Executive Order 13520, and Office of Management and Budget (OMB) guidance for the implementation of IPERA. DHS intends the *Guidebook* to be a living document, and it released the latest version, 1.2, in May 2011.

The diagram below shows the process DHS Components are required to follow to identify, estimate, report, and recover improper payments:



Source: DHS-OIG illustration of processes based on information in DHS Improper Payments Reduction Guidebook, Office of Chief Financial Officer (OCFO) Internal Control Program Management Office.

IPERA also requires agencies' Inspectors General to determine and report annually on whether the agency is in compliance with IPERA. This report meets that requirement.

Results of Audit

To comply with IPERA, an agency is required to conduct risk assessments and report and publish the results of selected program testing in its *Annual Financial Report*. The agency must also report improper payment rates of less than 10 percent for each program. KPMG LLP (KPMG) did not find any instances of noncompliance with IPERA.

Additionally, we reviewed the processes and procedures by which DHS estimates its annual improper payment rates. Based on our review, we determined that DHS needs to 1) improve controls to ensure completeness and accuracy of reporting and 2) increase efforts to recover improper payments.

DHS' Compliance with IPERA

We contracted with KPMG to determine whether DHS complied with IPERA in FY 2011. KPMG conducted audit procedures to determine if DHS met the following requirements prescribed in the Act:

- conducted required program-specific risk assessments;
- published improper payment estimates for high-risk programs;
- published programmatic corrective action plans;
- published, and has met, annual reduction targets for programs at risk;
- achieved and reported a gross improper payment rate of less than 10 percent for all programs tested; and
- reported on its efforts to recover improper payments.

KPMG did not find any instances of noncompliance with the Act.

DHS' Controls over Improper Payment Testing and Reporting

DHS needs to improve its controls over improper payment testing and reporting. Specifically, DHS needs to improve its review process to ensure that all payments are included, subject to testing, and reported. Further, DHS needs to improve its policies and procedures and adequately segregate duties.

Payments Excluded from Testing and Reporting

For each high-risk program, the DHS *Guidebook* requires that Components provide DHS OCFO with the list of payments made during the fiscal year. DHS' Internal Control and Risk Management Office (ICRM) then selects a statistically valid sample of the payments and reviews the related files for improper

payments. CBP mistook some payments from its Security Border Fencing Program as adjustments, and excluded them from the list of payments provided to DHS OCFO.

OMB Circular A-123, *Management's Responsibility for Internal Control*, requires management to develop and maintain effective internal controls over financial reporting. DHS did not detect the exclusion of payments during its review process and before it published its FY 2011 AFR. As a result, the total amount of payments subjected to selection for testing and the amount reported for this program in the FY 2011 AFR are understated by approximately \$85 million.

Subsequent to DHS publishing its FY 2011 AFR, CBP tested the excluded payments and identified four payments totaling \$16,514, which should have been reported as improper payments.

Inaccurate Payment Recovery Audit Reporting

DHS inaccurately reported the amount subject to review and the actual amount reviewed in its payment recovery audit reporting in its FY 2011 AFR. Specifically, DHS included Federal Protective Services' payments, totaling \$813 million, under ICE rather than NPPD. As discussed above, OMB Circular A-123, *Management's Responsibility for Internal Control*, requires management to develop and maintain effective internal controls over financial reporting. DHS did not effectively perform its review function to detect and correct the error. Including inaccurate data in the AFR could mislead users of that data.

Independence

Components are required to perform testing of a sample of payments to determine whether payments are improper. The DHS ICRM is responsible for ensuring the Department's and Components' compliance with IPERA. The ICRM provides guidance and is responsible for approving Component test plans and other IPERA-related activities. As part of its oversight of the process, ICRM personnel are also responsible for reviewing a sample of payments tested by Components in order to ensure that their test results are reliable.

The Director of Internal Controls and the Program Analyst in the ICRM have performance goals of retesting IPERA test work conducted by Components. These personnel also have a

conflicting performance goal of reducing improper payments. Similar conflicts exist at CBP and FEMA. OMB Circular A-123 provides that control activities include policies, procedures, and mechanisms in place to ensure that agencies meet their objectives. This includes proper segregation of duties. Segregating the duties designed to 1) reduce improper payments and 2) test payments files for improper payments will promote independence and reduce the risk of inaccurate or incomplete improper payment data.

Improve DHS Guidance

DHS' *Improper Payments Reduction Guidebook* provides guidance to Components for IPERA-related activities, including assessing risk, testing for improper payments, and reducing and recapturing improper payments. OMB Circular A-123 provides that control activities include policies and procedures to ensure that agency objectives are met. Based on our review, the guidance needs to clarify how to apply the results when a Component uses an alternate testing methodology.

Alternate Sampling Methodology

The prescribed OMB sampling methodology presumes that all program payments will be subject to selection for testing for improper payments. Exceptions from prescribed OMB sampling methodology are permitted, but the guidance does not differentiate how the results from such sampling should be applied. Consequently, high-risk programs may not be tested in the future and corrective actions may not be monitored.

FEMA received permission from OMB to use an alternative methodology for three grant programs: Public Assistance, Homeland Security, and Transit Security.⁴ Each program reported estimated improper payments of less than \$1 million and error rates of less than one percent as a result of the limited testing conducted under the alternative methodology. FEMA did not draft mission action plans (MAPs) for Transit Security or Homeland Security Grant Programs because neither reported more than \$10 million in improper payments. MAPS are a management tool to address and remedy identified internal control deficiencies such as improper payments. Additionally, FEMA intends to ask for a

⁴ The scope of the assessment for the Public Assistance Grant Program was limited to targeted transactions from FEMA Regions I, II, III, and X. Testing for the Homeland Security Grant Program was based on a targeted sample of the largest payments disbursed in 17 states. Testing for the Transit Security Grant Program was based on a targeted sample of payments in 9 states.

waiver from further testing of the Transit Security Grant Program because of its low error rate.

DHS' guidance does not address how to treat results of testing that deviate from OMB methodology. Without this guidance, programs that should be tested may not be tested and MAPS, with monitored corrective actions, may not be developed.

Recommendations

We recommend that the Deputy Chief Financial Officer, Department of Homeland Security:

Recommendation #1: To ensure that all payments for programs and activities identified as high risk are subject to selection for testing and reported, the Department must:

- Enhance controls and processes used by Components to reconcile their lists of fiscal year payments with their financial accounting system; and
- Enhance controls and processes used by the Department of Homeland Security to review Components' lists of fiscal year payments to ensure that they are complete and that variances are investigated, accounted for, and substantiated.

Recommendation #2: Include the following corrections in the Department of Homeland Security's FY 2012 *Annual Financial Report*:

- FY 2011 recovery audit reporting for Federal Protective Services under National Protection & Programs Directorate; and
- Excluded payments from U.S. Customs and Border Protection's Secure Border Fencing program from the FY 2011 *Annual Financial Report*.

Recommendation #3: Develop and implement procedures to ensure that duties to determine the level of improper payments and to reduce improper payments are adequately segregated.

Recommendation #4: Modify the Department of Homeland Security's *Improper Payment Reduction Guidebook* to provide guidance to Components on how to treat results of testing using alternative methodologies. When seeking approval from the Office of Management and Budget for an alternate sampling methodology, DHS shall propose dollar thresholds that will be

applicable to the results of testing using approved alternate sampling methodology.

DHS' Efforts to Recover Improper Payments

DHS needs to improve its improper payment recovery efforts. Not all Components conducted payment recovery audits as required by IPERA. Of those Components that did conduct recovery audits, only the USCG prioritized its audit to target categories with higher potential for overpayments and recoveries. If these issues are corrected, DHS would benefit by recovering a greater number of improper payments.

Performing Recovery Audits

DHS decided not to perform recovery audits for the Domestic Nuclear Detection Office (DNDO) and TSA. By not performing the required recovery audits, DHS potentially missed an opportunity to recover improper payments. USCG provides financial services for DNDO and TSA, and a USCG general recovery audit contract would include payments made by these Components. In FY 2011, DHS and USCG decided that a targeted recovery audit of USCG telecommunication invoices would be of greater benefit to the government than a general recovery audit of all USCG-processed payments. In its FY 2011 AFR, DHS reported that in FY 2012 it plans to conduct a general recovery audit for DNDO and TSA covering FY 2010 and FY 2011 contract payments. The U.S. Secret Service (USSS) did not conduct a recovery audit because it did not enter into a recovery audit contract in time to perform an audit in FY 2011. Previously, agencies had to conduct recovery audits for each program and activity that expended at least \$500 million. The USSS did not have to conduct recovery audits under the \$500 million threshold, but its programs fell within IPERA's lower \$1 million threshold. DHS plans to conduct a general recovery audit in FY 2012 for USSS covering FY 2010 and FY 2011 contract payments.

A payment recovery audit is designed to identify overpayments by reviewing accounting and financial records, supporting documentation, and other information. IPERA requires an "agency to conduct recovery audits with respect to each program and activity of the agency that expends \$1 million or more annually if conducting such audits would be cost-effective." In FY 2010, DNDO paid approximately \$369 million, TSA paid approximately \$2.18 billion, and USSS paid approximately \$393 million in contract payments. Despite exceeding IPERA's \$1 million

threshold, none of these Components conducted a payment recovery audit in FY 2011.

Targeting High-Risk Payments for Recovery Audits

OMB requires agencies to prioritize payment recovery audits on categories that have a higher potential for overpayments and recoveries. For CBP, FEMA, ICE, Management, NPPD, Office of Health Affairs, S&T, and U.S. Customs and Immigration Service, the recovery auditors reviewed the entire population of contract payments rather than focusing on categories that are higher risk or have a higher potential for overpayment and recoveries. These recovery audits, which reviewed more than \$8 billion, identified \$73,000 in recoverable overpayments.

USCG's recovery audit, which focused on telecommunication invoices, was the exception. USCG targeted telecommunications invoices because of the carriers' complex pricing and billing practices. The recovery audit examined \$78 million in payments and identified errors totaling more than \$4 million. Furthermore, DHS reported an immediate cost savings of \$102,355 and estimated future cost savings in excess of \$2 million. By using a targeted approach, USCG's recovery audit identified more errors than those of other Components despite reviewing fewer payments. Although ICE, CBP, and FEMA conducted general recovery audits, there is no evidence to indicate that these Components targeted certain payment types. While general recovery audits are important, targeted, in-depth recovery audits could potentially identify and recover substantially more improper payments.

OMB places responsibility for prioritizing recovery audits on the agencies. DHS' Payment Recapture Audit Plan assigns this responsibility to the recovery auditors. Components are to provide 100 percent of their contract payments to recovery audit contractors. The recovery audit contractors then use proprietary software to identify and focus on categories at higher risk of improper payments and on identifying whether certain types of improper payments have occurred, such as duplicate payments. The focus of the recovery audit is set by the proprietary software as opposed to a targeting of high-risk payments prioritization by DHS.

Recommendations

We recommend that the Deputy Chief Financial Officer, Department of Homeland Security, ensure that:

Recommendation #5:

- Domestic Nuclear Detection Office, the Transportation Security Administration, and U.S. Secret Service conduct recovery audits as planned and reported in the Department's FY 2011 *Annual Financial Report*; and
- Components follow the requirements of the *Improper Payments Elimination and Recovery Act of 2010* to perform recovery audits annually if conducting such recovery audits is cost-effective.

Recommendation #6:

- Components target those improper payment categories that have a higher potential for overpayment and recoveries for recovery audits, when cost-effective; and
- Modify the Department of Homeland Security's Payment Recapture Audit Plan to follow OMB guidance for prioritizing recovery audits.

Management Comments and OIG Analysis

DHS concurred with all six of our recommendations. DHS provided a description of actions already taken and planned actions to be completed before or by November 2012. Based on the information provided by DHS on February 27, 2012, recommendation #1 is closed. Recommendations 2 through 6 are resolved and will remain open until we verify that DHS has implemented these recommendations. We included a copy of the management comments in their entirety in appendix B.

Management Response to Recommendation #1

DHS concurs with this recommendation. DHS reports that it has taken action to address this recommendation. Specifically, ICRM staff included additional controls to the template that will be submitted by Components to identify and reconcile program payment populations to Treasury disbursement totals. By having Components complete quality assurance questions that were previously performed by ICRM staff, problems will be identified earlier thus allowing more time to promptly and properly resolve

them. ICRM personnel are now required to review transactions identified as non-payment on the Components' disbursement general ledger.

OIG Analysis: On February 27, 2012, DHS provided its updated DHS *Improper Payment Reduction Guidebook*, version 2.0, which includes the updated program identification template with program identification checklist that Components are required to complete.

The updated guidance also requires Components to provide payment detail files for all payments listed on the program identification template, and payment detail files for any non-payment entries. The previous guidance required the payment detail files for payments only. During our audit, we noted that some payments were excluded from the list of CBP Security Border Fencing program payments because they appeared to be journal entries. This new requirement should provide DHS with support for all payments or entries to ensure a complete list of program payments.

We consider DHS' actions responsive. Based on our review of documentation provided by DHS in support of the described actions this recommendation is closed.

Management Response to Recommendation #2

DHS concurs with this recommendation.

OIG Analysis: This recommendation is resolved and will remain open until we are able to verify the corrections in DHS' FY 2012 *Annual Financial Report*, which is required to be published by November 2012.

Management Response to Recommendation #3

DHS concurs with this recommendation. DHS plans to 1) update its *Improper Payments Reduction Guidebook*; 2) provide training to ensure that improper payment reviewers are not directly involved in processing any payments they are asked to review; and 3) assign payment review to individuals who do not have a performance measure goal to reduce improper payments.

OIG Analysis: With respect to DHS' plan to assign payment review to individuals who do not have a performance measure goal to reduce improper payments, we offer some clarification. The

task of reviewing payment files for improper payments must not be conducted by personnel responsible for reducing improper payments for that same program. Simply, personnel should not test their own work. Furthermore, personnel conducting the review of payments should not report to someone who is responsible for keeping improper payment rates low.

This recommendation has been addressed partially by the additional instruction to Components in DHS' *Improper Payment Reduction Guidebook*, version 2.0. The *Guidebook* provides that personnel reviewing payment files for IPERA purposes must not review payments files for payments they are directly involved in processing. This recommendation is resolved and will remain open until DHS completes the remaining actions described.

Management Response to Recommendation #4

DHS concurs with this recommendation. ICRM staff will update the DHS *Improper Payments Reduction Guidebook* to explicitly state that the Department's practice of applying the \$10 million estimated error reporting threshold shall apply to programs using the standard methodology. When seeking approval from the Office of Management and Budget for an alternate sampling methodology, DHS will include dollar thresholds applicable to the results.

OIG Analysis: DHS and FEMA are currently using a multi-year alternate sampling methodology plan, approved by OMB, for which the Department does not need annual approval. The revised guidance should apply to new DHS requests for approval to use alternate methodologies. This recommendation is resolved and will remain open until implemented.

Management Response to Recommendation #5

DHS concurs with this recommendation. DHS plans to ensure that DNDO and TSA recovery audit work will be conducted by the Comptroller of the USCG during FY 2012, as planned and reported in DHS' FY 2011 *Annual Financial Report*. The USSS' Chief Financial Officer will also complete recovery audit work in FY 2012.

OIG Analysis: This recommendation is resolved and will remain open until DHS provides documentation supporting that recovery audits were completed in FY 2012 for DNDO, TSA, and USSS.

Management Response to Recommendation #6

DHS concurs with this recommendation. DHS plans to revise its *Improper Payments Reduction Guidebook* and related training. The revised version will emphasize the need for Component contracting officer representatives to provide recovery audit contractors with direction and explanation on targeting the highest known or suspected payment risks.

OIG Analysis: This recommendation is resolved and will remain open until DHS completes this work and provides documentation in support of the actions taken.

Appendix A

Purpose, Scope, and Methodology

The audit objectives were to 1) determine the Department of Homeland Security's compliance with the *Improper Payments Elimination and Recovery Act of 2010*; 2) evaluate the accuracy and completeness of DHS' improper payment reporting; and 3) evaluate DHS' performance in reducing and recapturing improper payments.

The scope of the audit is DHS' FY 2011 efforts to comply with IPERA. We limited our scope to certain DHS Components. Using DHS' *Annual Financial Reports* from FY 2008 through 2010, we judgmentally selected Components to review because they reported programs as high risk for improper payments. The Components we selected are U.S. Coast Guard, U.S. Customs and Border Protection, Federal Emergency Management Agency, U.S. Immigration and Customs Enforcement, and Transportation Security Administration. Additionally, we included National Protection and Programs Directorate and Science and Technology Directorate because DHS listed them in FY 2011 High Dollar Overpayment reports.

To understand DHS' requirements under IPERA and DHS' policies and procedures to meet those requirements, we obtained and reviewed relevant authorities and guidance including IPERA, OMB's memorandum on implementing IPERA, and DHS' *Improper Payment Reduction Guidebook*. We also interviewed officials in DHS' Office of Chief Financial Officer and the various Components directly involved with IPERA implementation.

We contracted with independent auditor KPMG to determine DHS compliance with IPERA. The contract required that KPMG perform its audit in accordance with generally accepted government auditing standards. Those standards require that the auditors plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for their findings and conclusions based upon the audit objectives.

At each Component, KPMG performed the following:

- Obtained and read relevant authorities and guidance;
- Interviewed Component management and reviewed Component policies;
- Reviewed Components' risk assessment processes;
- Reviewed Components' sampling plans and methodologies; and
- Reviewed Components' corrective action plans.

Appendix A

Purpose, Scope, and Methodology

At DHS, KPMG reviewed DHS' FY 2011 AFR to determine compliance with reporting requirements.

To evaluate the accuracy and completeness of DHS' improper payment reporting, we performed the following procedures:

- Reviewed Components' risk assessments;
- Reconciled Components' risk assessments with FY 2010 gross disbursement data;
- Reviewed sample test plans and results; and
- Reviewed DHS' internal controls over the processes and procedures used to estimate the improper payment rate, including the risk assessment process, testing, and reporting.

We did not conduct any sample payment testing to validate DHS' estimated improper payment rates reported in the FY 2011 AFR.

To evaluate DHS' performance in reducing and recapturing improper payments, we performed the following procedures:

- Reviewed DHS' FY 2011 AFR for improper payment reduction and recovery data;
- Reviewed DHS' corrective action plans; and
- Reviewed recovery auditors' reports.

We conducted this performance audit between September 2011 and January 2012 pursuant to the *Inspector General Act of 1978*, as amended, and according to generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based upon our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based upon our audit objectives.

Appendix B
Management Comments to the Draft Report


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



**Homeland
Security**

FEB 23 2012

MEMORANDUM FOR: Anne L. Richards
Assistant Inspector General for Audits

FROM: 
Peggy Sherry
Deputy Chief Financial Officer

SUBJECT: Department of Homeland Security's Compliance with the
Improper Payments Elimination and Recovery Act of 2010
(Project No. 11-044-AUD-MGMT)

Thank you for the opportunity to review and comment on this draft report. We appreciate the Office of Inspector General's (OIG) work conducting its statutorily-required annual review of the U.S. Department of Homeland Security's (DHS) compliance with the Improper Payments Elimination and Recovery Act of 2010 (IPERA) and issuing this report.

We are pleased to note that KPMG LLP, the Department's independent financial statements auditor, did not find any instances of noncompliance with the Act. We also welcome the OIG's positive recognition of actions taken by the U.S. Coast Guard that focused on targeting high-risk telecommunications payments for recovery audits and which resulted in immediate cost savings of \$102,355 and estimated future cost savings of more than \$2 million. We consider this work a government-wide best practice and are expanding it to other Components in FY 2012.

We have achieved many additional successes related to the Department's improper payments work. For example, the Federal Emergency Management Agency (FEMA) has consistently lowered the estimated error rate for its high-risk programs. The overall error rate for FEMA's high-risk programs dropped from 8.0% reported in FY 2009 to 1.7% in FY 2010 to 1.0% in FY 2011. This improvement was driven by the staff of the FEMA Office of the Chief Financial Officer who led mission action plan completion and formed successful partnerships with FEMA grant program managers. Improvements include adding applicant eligibility edit checks, standardizing documentation requirements, and providing training on the root causes of errors and steps to address payment risks. Additionally, the staff of the DHS Office of the Chief Financial Officer (OCFO) fully engaged with staff from the DHS Office of the Chief Procurement Officer and leveraged their expertise when evaluating contract payments. This cooperation improves our reporting and assists the development of mission action plans by ensuring that the root causes behind improper payment risk and contract management weakness are addressed.

Appendix B

Management Comments to the Draft Report

Your report contained six recommendations, with which the Department concurs. Specifically, you recommended the following actions to the Deputy Chief Financial Officer:

Recommendation #1: To ensure that all payments for programs and activities identified as high risk are subject to selection for testing and reported, the Department must:

- (1) Enhance controls and processes used by Components to reconcile their lists of fiscal year payments with their financial accounting system; and
- 2) Enhance controls and processes used by the Department of Homeland Security to review Components' lists of fiscal year payments to ensure that they are complete and that variances are investigated, accounted for, and substantiated.

Response: Concur. DHS has taken action to address this recommendation. Specifically, additional controls were added by Internal Control and Risk Management (ICRM) staff to the template which will be submitted by Components to identify and reconcile program payment populations to Treasury disbursement totals. By having Components complete quality assurance questions which were previously performed by ICRM staff, problems will be identified earlier thus allowing more time to promptly and properly resolve them. Controls were also added to require ICRM staff to review transactions identified by Components as non-payment which updated disbursement general ledger accounts. We request this recommendation be considered closed. (Completion Date: December 27, 2011)

Recommendation #2: Include the following corrections in the Department of Homeland Security's FY 2012 *Annual Financial Report*:

- (1) FY 2011 recovery audit reporting for Federal Protective Services under National Protection & Programs Directorate; and
- (2) Excluded payments from U.S. Customs and Border Protection's Secure Border Fencing program from the FY 2011 *Annual Financial Report*.

Response: Concur. These corrections will be clearly noted in the FY 2012 *Annual Financial Report*. We request this recommendation be considered resolved and open, pending final publication of the FY 2012 report. (Estimated Completion Date: November 15, 2012)

Recommendation #3: Develop and implement procedures to ensure that duties to determine the level of improper payments and to reduce improper payments are adequately segregated.

Response: Concur. ICRM staff will: (1) update the *Improper Payments Reduction Guidebook* (Guidebook), (2) provide training to ensure that improper payment reviewers are not directly involved in processing any payments they are asked to review and (3) assign payment reviews to individuals who do not have a performance measure goal to reduce improper payments. The updated Guidebook will more prominently emphasize that improper payment test documentation must be complete and transparent. We request this recommendation to be considered resolved and open, pending updating of the Guidebook, completion of related training, and independent

Appendix B

Management Comments to the Draft Report

review of Component sample test results by ICRM staff. (Estimated Completion Date: September 30, 2012)

Recommendation #4: Modify the Department of Homeland Security's *Improper Payments Reduction Guidebook* to provide guidance to Components on how to treat results of testing using alternative methodologies. When seeking approval from the Office of Management and Budget for an alternate sampling methodology, DHS shall propose dollar thresholds that will be applicable to the results of testing under an approved alternate sampling methodology.

Response: Concur. The Guidebook will be updated by ICRM staff to explicitly state the Department's practice of applying the ten million dollar estimated error reporting threshold required of programs not using alternative methodologies to all national estimates in cases where an alternate sampling methodology is employed. When seeking approval from the Office of Management and Budget for an alternate sampling methodology, DHS will include dollar thresholds applicable to the results. Please note that the approval received from the Office of Management and Budget for FEMA's use of an alternate sampling methodology, established a multi-year testing and reporting methodology which does not require annual approval. We request this recommendation to be considered resolved and open, pending ICRM's updating of the Guidebook. (Estimated Completion Date: February 29, 2012)

Recommendation #5: Ensure that the Domestic Nuclear Detection Office, the Transportation Security Administration, and U.S. Secret Service conduct recovery audits as planned and reported in the Department's FY 2011 Annual Financial Report; and Components follow the requirements of the Improper Payments Elimination and Recovery Act of 2010 to perform recovery audits annually if conducting such recovery audits is cost-effective.

Response: Concur. Planned Domestic Nuclear Detection Office and Transportation Security Administration recovery audit work will be completed by the Comptroller of the U.S. Coast Guard during FY 2012. The U.S. Secret Service's Chief Financial Officer will also complete recovery audit work during the same time period. We request this recommendation to be considered resolved and open, pending completion of this work. (Estimated Completion Date: September 30, 2012)

Recommendation #6: Ensure that Components target those improper payment categories that have a higher potential for overpayment and recoveries for recovery audits, when cost-effective and modify the Department of Homeland Security's Payment Recapture Audit Plan to follow OMB guidance for prioritizing recovery audits.

Response: Concur. The Department is strongly committed to maximizing the effectiveness and efficiency of every taxpayer dollar we receive. ICRM staff will review the Guidebook and related training to ensure it emphasizes the need for Component contracting officer representatives to provide recovery audit contractors with direction and explanation on targeting the highest known or suspected payment risks (as required by OMB guidance). For example, as a result of increased emphasis in this area, DHS is planning to expand targeted recovery audit work on telecommunications payments. We request this recommendation to be considered

Appendix B

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resolved and open, pending completion of this work. (Estimated Completion Date: September 30, 2012)

Again, thank you for the opportunity to review and comment on this draft report. In particular, I appreciate the high level of communication exhibited between your audit team and my staff during the audit. By necessity, the time available to complete this audit was relatively short, yet your team provided highly beneficial feedback throughout the entire engagement. As a result, we have already taken concrete steps to address most of the findings and have a clear path to achieve full resolution of the remaining findings. We look forward to working with you on future Homeland Security issues.

Appendix C
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The Committee on Homeland Security and Governmental Affairs
of the Senate
The Committee on Oversight and Governmental Reform of the
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