



Department of Homeland Security Office of Inspector General

Office of Financial Management's Management Letter for FY 2010 DHS Consolidated Financial Statements Audit





Homeland
Security

MAR 7 2011

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 Office of Financial Management's Management Letter for FY 2010 DHS Consolidated Financial Statements Audit. It contains observations related to internal control that were not required to be reported in the financial statement audit report. The independent public accounting firm KPMG LLP (KPMG) performed the integrated audit of DHS' FY 2010 financial statements and internal control over financial reporting and prepared this management letter. KPMG is responsible for the attached management letter dated February 2, 2011, and the conclusions expressed in it. We do not express opinions on DHS' financial statements or internal control, nor do we provide conclusions on compliance with laws and regulations.

The observations herein 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 handwritten signature in cursive script that reads "Anne L. Richards".

Anne L. Richards
Assistant Inspector General for Audits



KPMG LLP
2001 M Street, NW
Washington, DC 20036-3389

February 2, 2011

Office of Inspector General
U.S. Department of Homeland Security, and
Chief Financial Officer
U.S. Department of Homeland Security
Washington, DC

Ladies and Gentlemen:

We were engaged to audit the balance sheet of the U.S. Department of Homeland Security (DHS or Department) as of September 30, 2010 and the related statement of custodial activity for the year then ended (referred to herein as “financial statements”). We were also engaged to examine the Department’s internal control over financial reporting of the balance sheet as of September 30, 2010, and the statement of custodial activity for the year then ended. We were not engaged to audit the accompanying statements of net cost, changes in net position, and budgetary resources for the year ended September 30, 2010 (referred to herein as other fiscal year (FY) 2010 financial statements), or to examine internal control over financial reporting over the other FY 2010 financial statements.

Because of matters discussed in our *Independent Auditors’ Report*, dated November 12, 2010, the scope of our work was not sufficient to enable us to express, and we did not express, an opinion on the FY 2010 financial statements and we were unable to perform procedures necessary to form an opinion on DHS’ internal control over financial reporting of the balance sheet as of September 30, 2010 and the related statement of custodial activity for the year then ended.

The Office of Financial Management (OFM) is part of DHS. We noted certain matters involving internal control and other operational matters, related to OFM that are summarized in the Table of Financial Management Comments on the following pages, and presented for your consideration in Section I of this letter. These comments and recommendations, all of which have been discussed with the appropriate members of management, are intended to improve internal control or result in other operating efficiencies. These comments are in addition to the significant deficiencies presented in our *Independent Auditors’ Report*, dated November 12, 2010, included in the FY 2010 DHS *Annual Financial Report*. A description of each internal control finding and its disposition as either a significant deficiency or a financial management comment is provided in Appendix A.

As described above, the scope of our work was not sufficient to express an opinion on the balance sheet as of September 30, 2010 or the statement of custodial activity of DHS for the year then ended, and we were not engaged to audit the statements of net cost, changes in net position, and budgetary resources for the year ended September 30, 2010. Accordingly, other internal control matters may have been identified and reported had we been able to perform all procedures necessary to express an opinion on the FY 2010 financial statements and had we been engaged to audit the other FY 2010 financial statements. We aim, however, to use our knowledge of DHS’ organization gained during our work to make comments and suggestions that we hope will be useful to you.



We would be pleased to discuss these comments and recommendations with you at any time. This report is intended for the information and use of DHS' management, the DHS Office of Inspector General, the U.S. Office of Management and Budget, the U.S. Congress, and the Government Accountability Office, and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

KPMG LLP

Department of Homeland Security
Table of Financial Management Comments
September 30, 2010

TABLE OF FINANCIAL MANAGEMENT COMMENTS (FMC)

Comment Reference	Subject	Page(s)
FMC 10-01	Tracking System for Ethics Training, Public Financial Disclosures, and Confidential Reports	2
FMC 10-02	Preparation of the Departmental Interim Legal Letter	2
FMC 10-03	SAS 70 Rollforward Procedures	3
FMC 10-04	Discrepancies Exist Between DHS Guidance and the Treasury Information Executive Repository (TIER) Analytical Report	3

APPENDIX

Appendix	Subject	Page(s)
A	Crosswalk – Financial Management Comments to Active NFRs	4
B	Status of Prior Year NFRs	5-6

Department of Homeland Security
Financial Management Comments
September 30, 2010

FMC 10-01 – Tracking System for Ethics Training, Public Financial Disclosures, and Confidential Reports (NFR No. CONS 10-01)

During our testwork over entity-level controls, we noted that DHS had not finalized and issued procedural guidance for financial disclosure reporting and department-wide supplemental ethics guidance, including the DHS' supplemental Standards of Conduct. Additionally, DHS did not have a single, department-wide system to record and monitor required ethics training and to record the positions that required their incumbents to file financial disclosure reports. Consequently, DHS was unable to monitor the filing status of all required reports.

Recommendations:

We recommend that the Designated Agency Ethics Official (DAEO), in conjunction with the Chief Human Capital Officer and the Chief Information Officer, as appropriate:

- Continue to work to issue procedural guidance for financial disclosure reporting, the Secretary's Statement on Standards of Conduct, and the Department's supplemental ethics directive.
- Continue to develop and implement a department-wide system to ensure all employees who must complete financial disclosure reports/receive mandatory ethics training are identified and meet the requirements.

FMC 10-02 – Preparation of the Departmental Interim Legal Letter (NFR No. CONS 10-02)

DHS's Office of General Counsel (OGC) did not maintain a central database, which stores a comprehensive list of all legal cases, that was readily available upon request. Although some components maintain their own database, others need to request a data call in order to analyze and respond to a legal request. However, we noted that OGC was able to represent, through its knowledge of the pending cases and historical payouts, that the likelihood of loss from cases not aggregated in the legal letter is immaterial to the financial statements.

Recommendations:

We recommend that DHS:

- Update current policies and procedures to emphasize the need for thorough, complete, and accurate data.
- Update legal liability workshops to include activities focused on completeness of component legal liability data.
- Conduct a Department-wide risk assessment on legal liability processes at components. Analyze results and develop mission action plans to target high risk areas.
- If available, pursue opportunities to implement a department-wide automated system or database.

Department of Homeland Security
Financial Management Comments
September 30, 2010

FMC 10-03 – SAS 70 Rollforward Procedures (*NFR No. CONS 10-05*)

During FY 2010, DHS did not have policies and procedures to perform or document a period update, from the SAS 70 report issuance date to the DHS balance sheet date. In addition, no period update from the SAS 70 report issuance date to the DHS balance sheet date was documented for USDA's National Finance Center's control environment.

Recommendation:

We recommend that DHS revise its guidance to include the rollforward period for SAS 70 reports.

FMC 10-04 – Discrepancies Exist Between DHS Guidance and the Treasury Information Executive Repository (TIER) Analytical Report (*NFR No. CONS 10-08*)

We identified the following exception upon comparing the DHSTIER Analyt2 Table and the OFM Analytics Guidance Documents:

- General Fund's Analytic #2: (Budgetary Cash = Proprietary Cash - Activity (Direct Method)) was inappropriately configured.

"Budgetary Cash = Proprietary Cash - Activity (Direct Method)," includes the year-to-date activity (A) for account 4176, calculated as the difference between ending balance and beginning balance. However, the analytic incorrectly calculates this as the sum of the ending and beginning balances for account 4176

Recommendation:

We recommend that DHS OFM modify the DHSTIER Specification Table to be consistent with the USSGL guidance relating to Tie-Points, and ensure that the analytic formulas are accurate and complete.

Department of Homeland Security
 Crosswalk - Financial Management Comments to NFRs
 September 30, 2010

NFR No.	Description	Disposition ¹			
		IAR			FMC
		MW	SD	NC	No.
10-01	Tracking System for Ethics Training, Public Financial Disclosures, and Confidential Reports				10-01
10-02	Preparation of the Departmental Interim Legal Letter				10-02
10-03	Audited Financial Statements			J, L	
10-04	<i>Number not used</i>	Not applicable			
10-05	Lack of SAS 70 Rollforward Guidance				10-03
10-06	Compliance with OMB Circular A-136			N	
10-07	Statement of Net Cost (SNC) Methodologies and IT Systems Functionality			J	
10-08	Discrepancies Exist Between DHS Guidance and the TIER Analytical Report				10-04
10-09	<i>Number not used</i>	Not applicable			
10-10	Non-compliance with OMB Circular A-50, <i>Audit Follow-up</i>			I	
10-11	Preparation and Review of the Special-Purpose Financial Statements and Notes	Note 1			

¹Disposition Legend:

IAR	Independent Auditors' Report dated November 12, 2010
FMC	Financial Management Comment
MW	Contributed to a Material Weakness at the Department level when combined with the results of all other components
SD	Contributed to a Significant Deficiency at the Department level when combined with the results of all other components
NC	Contributed to Noncompliance with laws, regulations, contracts, and grant agreements at the Department level when combined with the results of all other components
NFR	Notice of Finding and Recommendation

Cross-reference to the applicable sections of the IAR:

A	Financial Management and Reporting
B	Information Technology Controls and System Functionality
C	Fund Balance with Treasury
D	Property, Plant, and Equipment
E	Actuarial and Other Liabilities
F	Budgetary Accounting
G	Other Entity-Level Controls
H	Custodial Revenue and Drawback
I	<i>Federal Managers' Financial Integrity Act of 1982 (FMFIA)</i> , and Laws and Regulations Supporting OMB Circular No. A-50, <i>Audit Followup</i> , as revised
J	<i>Federal Financial Management Improvement Act of 1996 (FFMIA)</i>
K	<i>Single Audit Act Amendments of 1996</i>
L	<i>Chief Financial Officers Act of 1990 (CFO Act)</i>
M	<i>Antideficiency Act</i> , as amended (ADA)
N	<i>Government Performance and Results Act of 1993 (GPRA)</i>

Note 1: This finding was reporting in the Independent Auditors' Report on the Special-Purpose Financial Statements

Department of Homeland Security
 Status of Prior Year NFRs
 September 30, 2010

NFR No.	Description	Disposition ¹	
		Closed ²	Repeat (2010 NFR No.)
09-01	<i>Number not used</i>	Not applicable	
09-02	Tracking System for Ethics Training, Public Financial Disclosures, and Confidential Reports		CONS 10-01
09-03	Audited Financial Statements		CONS 10-03
09-04	<i>Number not used</i>	Not applicable	
09-05	<i>Number not used</i>	Not applicable	
09-06	<i>Number not used</i>	Not applicable	
09-07	<i>Number not used</i>	Not applicable	
09-08	Review of Component Financial Information	X	
09-09	<i>Number not used</i>	Not applicable	
09-10	<i>Number not used</i>	Not applicable	
09-11	Lack of Department-wide Policies and Non-Compliance with the Debt Collection Improvement Act of 1996 (DCIA)	X	
09-12	<i>Number not used</i>	Not applicable	
09-13	Statement of Net Cost (SNC) Methodologies and IT Systems Functionality		CONS 10-07
09-14	<i>Number not used</i>	Not applicable	
09-15	Preparation of the Departmental Legal Letter		CONS 10-02
09-16	<i>Number not used</i>	Not applicable	
09-17	<i>Number not used</i>	Not applicable	
09-18	<i>Number not used</i>	Not applicable	
09-19	Non-Compliance with OMB Circular A-50, Audit Follow-up		CONS 10-10
09-20	<i>Number not used</i>	Not applicable	
09-21	<i>Number not used</i>	Not applicable	
09-22	<i>Number not used</i>	Not applicable	
09-23	Discrepancies Exist Between DHS Guidance and the TIER Analytical Report		CONS 10-08
09-24	<i>Number not used</i>	Not applicable	
09-25	Review of FECA Actuarial Liability	X	
09-26	<i>Number not used</i>	Not applicable	
09-27	Timely Documentation and Review of Intragovernmental Activity and Balances	X	
09-28	Review of 6/30 AFR	X	
09-29	Component Monitoring related to Review of GAO 2020 Checklists	X	
09-30	Compliance with OMB Circular A-136		CONS 10-06
09-31	Review of JVs and JV log	X	
09-32	Preparation and Review of the Special-Purpose Financial Statements and Notes		CONS 10-11

¹ KPMG was engaged to perform an audit over the DHS balance sheet and statement of custodial activity as of and for the year ended September 30, 2010, and was not engaged to perform an audit over the statement of net cost, statement of changes in net position, and statement of budgetary resources for the year ended September 30, 2010.

Department of Homeland Security
Status of Prior Year NFRs
September 30, 2010

In addition, we were engaged to follow up on the status of all active NFRs that supported significant deficiencies reported in KPMG's *Independent Auditors' Report* dated November 13, 2009.

² NFRs were closed either through remediation of the findings or we were not engaged to follow up on active NFRs that did not support significant deficiencies reported in KPMG's *Independent Auditors' Report* dated November 13, 2009.

Report Distribution

Department of Homeland Security

Secretary
Deputy Secretary
Chief of Staff
Deputy Chief of Staff
General Counsel
Executive Secretary
Director, GAO/OIG Liaison Office
Assistant Secretary for Office of Policy
Assistant Secretary for Office of Public Affairs
Assistant Secretary for Office of Legislative Affairs
Chief Financial Officer
Chief Information Officer

Office of Management and Budget

Chief, Homeland Security Branch
DHS OIG Budget Examiner

Congress

Congressional Oversight and Appropriations Committees, as appropriate



ADDITIONAL INFORMATION AND COPIES

To obtain additional copies of this report, please call the Office of Inspector General (OIG) at (202) 254-4100, fax your request to (202) 254-4305, or visit the OIG web site at www.dhs.gov/oig.

OIG HOTLINE

To report alleged fraud, waste, abuse or mismanagement, or any other kind of criminal or noncriminal misconduct relative to department programs or operations:

- Call our Hotline at 1-800-323-8603;
- Fax the complaint directly to us at (202) 254-4292;
- Email us at DHSOIGHOTLINE@dhs.gov; or
- Write to us at:
DHS Office of Inspector General/MAIL STOP 2600,
Attention: Office of Investigations - Hotline,
245 Murray Drive, SW, Building 410,
Washington, DC 20528.

The OIG seeks to protect the identity of each writer and caller.